

***United States Court of Appeals
for the Second Circuit***



APPELLEE'S BRIEF

74-1157

United States Court of Appeals
FOR THE SECOND CIRCUIT

Docket No. 74-1157

WILLIAM R. VAN GEMERT, ET AL.,

Plaintiffs-Appellants,

—against—

THE BOEING COMPANY AND THOMAS R. WILCOX,

Defendants-Appellees.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF NEW YORK

BRIEF FOR DEFENDANTS-APPELLEES

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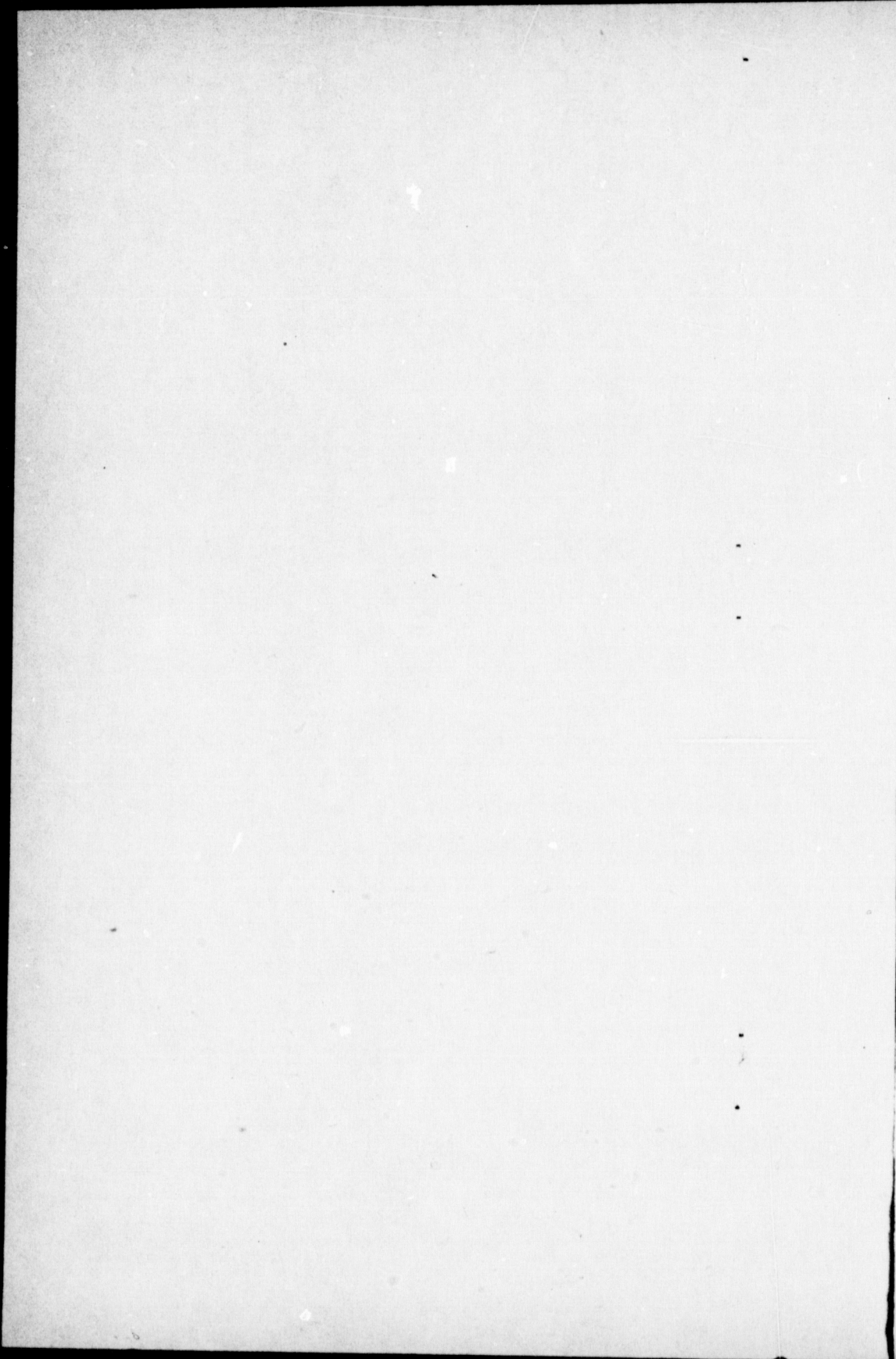


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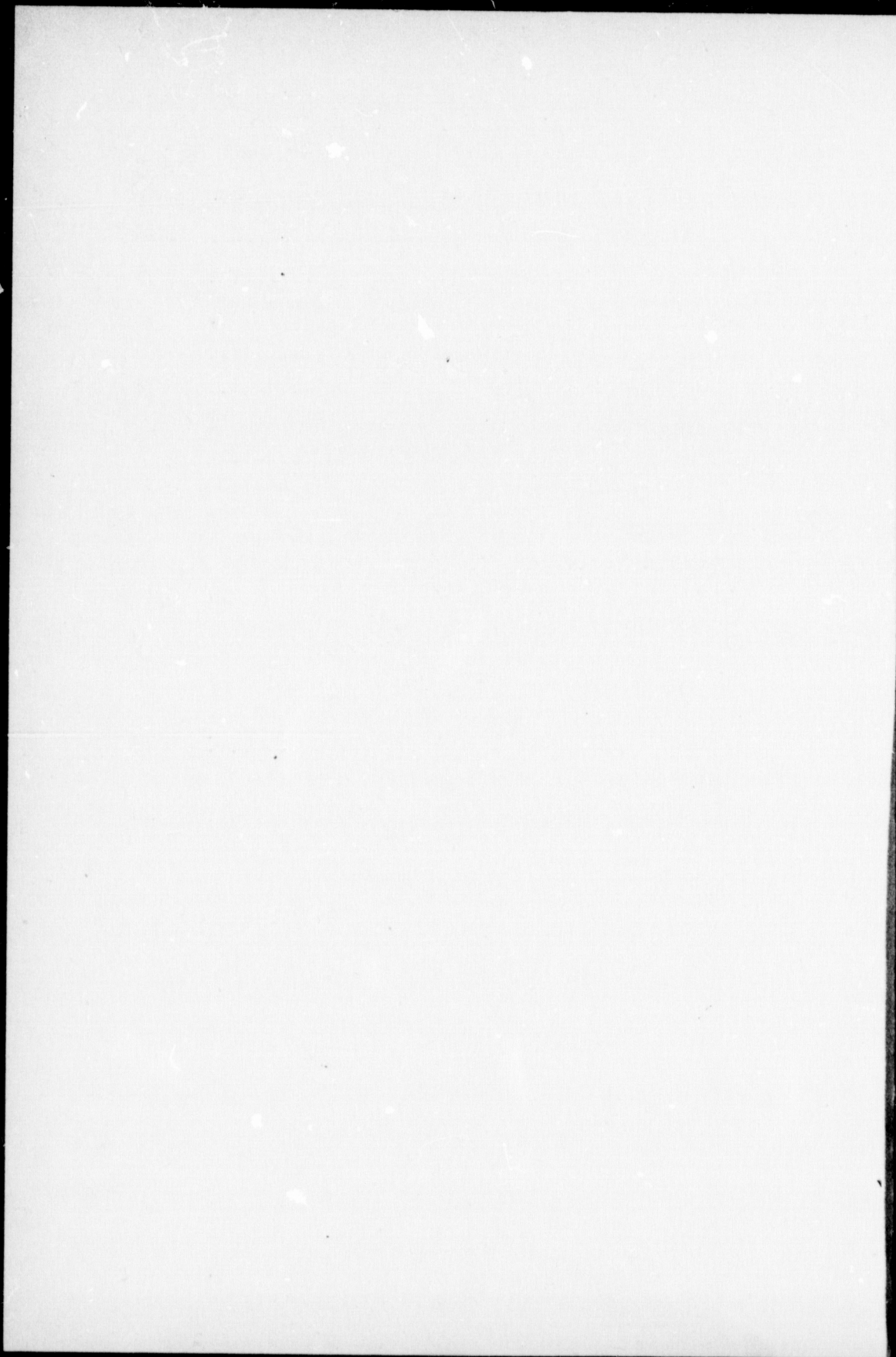
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DOCKET No. 74-1157

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—against—

THE BOEING COMPANY AND THOMAS R. WILCOX,

Defendants-Appellees.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF NEW YORK

BRIEF FOR DEFENDANTS-APPELLEES

Preliminary Statement

Plaintiffs appeal from a judgment of the United States District Court for the Southern District of New York, entered upon an agreed statement of fact and after a four-day trial in November, 1972, to the Hon. Sylvester J. Ryan. This judgment dismissed on the merits the complaints in ten consolidated actions which had been brought originally in 1966 against The Boeing Company ("Boeing"), all of its then directors and The Chase Manhattan Bank ("Chase") as trustee for Boeing's 4½% Convertible Sub-

ordinated Debentures due July 1, 1980 (the "debentures").

This is a consolidated class action¹ brought on behalf of all unregistered holders of Boeing's convertible debentures who failed to exercise their conversion privilege before it terminated on March 29, 1966, thus losing the market appreciation in their debentures for which they seek to recover damages in the amount of \$4,380,937.82 (285a).²

The Consolidated Complaint alleges, *inter alia*, that

(a) the notice given by Boeing in 1966 of the call of the debentures for redemption was legally insufficient;

(b) Boeing improperly calculated the conversion rate that was in effect at the time the debentures were called for redemption; and

(c) Boeing failed to comply with certain New York Stock Exchange ("NYSE") publicity procedures thus giving plaintiffs an implied cause of action under the Securities Exchange Act of 1934 (the "1934 Act")

¹ By order dated October 4, 1966, the District Court consolidated ten separate actions that had been commenced in various federal district courts and directed that they be maintained as a class action on behalf of all persons whose debentures were not surrendered for conversion on or before March 29, 1966 (75a-85a). Prior to trial Chase was dismissed from the case and none of the other defendants except for Boeing and Thomas R. Wilcox, one of its Directors, were ever served.

² Citations to Appellants' Appendix have the suffix "a". Exhibits not reproduced in the Appendix but contained in the separate volume of Exhibits to Agreed Statement As to Certain Facts and What Certain Witnesses Would Testify to If Called at Trial are indicated by "Ex. to ASOF." Citations to plaintiffs' two briefs, both undated and both denominated "Brief for Plaintiffs-Appellants", are indicated by "Winer Brief" for brief submitted by Nathan, Mannheimer, Asche, Winer & Friedman and "Kass Goodkind Brief" for brief submitted by Kass, Goodkind, Wechsler & Gerstein and others. For the convenience of the Court, the District Court's opinion is reproduced in the Appendix hereto.

and as third party beneficiaries of Boeing's Listing Agreement with the NYSE and the NYSE Company Manual (8a-40a).

The evidence before the Court was, for the most part, the agreed statement of facts (149a-219a) with oral testimony from Boeing's former President, its then Senior Vice President-Finance, its outside general counsel, a partner in its firm of independent auditors and from an expert accounting witness called by plaintiffs.

After its review of all the evidence presented and the legal arguments of the parties, the District Court rejected all of plaintiffs' claims holding that (a) "the notice of call was reasonable, valid and adequate" (303a); (b) the conversion rate in effect at the time of the call was correct (312a); and (c) there was "no merit or substance to plaintiffs' final point that the defendant BOEING breached a contract it had made with the New York Stock Exchange, in that it failed to comply with the publicity requirements of the Manual and/or the Listing Agreement" (312a).

To effect an orderly presentation, we shall in Argument *infra*, treat the three principal issues presented by plaintiffs' appeal in the order they were considered in the District Court's opinion.

Restatement of the Issues Presented by Plaintiffs

1. *Notice of the Call.* Whether the Court below was correct in holding that "the notice of call was reasonable, valid and adequate?"

2. *Conversion Rate.* Whether the Court below was correct in determining that Boeing properly calculated the

conversion rate that was in effect at the time the debentures were called for redemption?

3. *New York Stock Exchange Publicity Procedures.* Whether the Court below was correct (a) in finding that Boeing had complied with the publicity procedures of the NYSE and (b) in adhering to the uniform rule that, in any event, plaintiffs had no implied cause of action under the 1934 Act or as third party beneficiaries of Boeing's Listing Agreement and the NYSE Company Manual?

4. *Conduct of the Trial.* Whether in the way the Court below conducted the trial, it abused its discretion and deprived plaintiffs of a fair trial?

Restatement of the Case

The facts underlying the matters at issue on this appeal were largely stipulated by the parties prior to trial (*See ASOF at 149a et seq.*). There is no real dispute between the parties as to the record facts as set forth in the District Court's opinion (283a *et seq.*). At issue are some of the inferences, both factual and legal, that the District Court drew from the evidence.

A. The 1958 Offering

The debentures, which were issued in the aggregate principal amount of \$30,597,600, were registered with the SEC and listed on the NYSE. They were issued by Boeing in 1958 as part of a rights offering which was subscribed to by warrants (286a).

B. The Conversion Rate

The Indenture, which was entered into by Boeing and Chase as Trustee, provided in § 4.04 that the conversion

rate at which the debentures shall be converted into Boeing capital stock "shall be 2 shares of Capital Stock for each \$100 principal amount of Debentures, the conversion rate being subject to adjustment as hereinafter provided." (Ex. 4 to ASOF). The Indenture contains a formula for adjusting the conversion rate upon the possible occurrence of certain events (*Id.* at § 4.05).

It is of record and not in issue that the only three events that occurred between the time the debentures were issued in 1958 and the expiration of the conversion privilege on March 29, 1966, which might have affected the conversion rate were (a) the declaration by Boeing of a 4% Limited Stock Dividend³ in November, 1958; (b) the declaration by Boeing of a 2% Limited Stock Dividend in November, 1959; and (c) the issuance of Boeing capital stock in connection with the acquisition by Boeing of the assets of Vertol Aircraft Corporation ("Vertol") in 1960 (304a). With respect to the issuance of Boeing shares for the Vertol acquisition, § 4.05(b)(ii) of the Indenture provides that "the consideration other than cash shall be deemed to be the fair value thereof *as determined by the Board of Directors. . .*" (Ex. 4 to ASOF; emphasis added).

It is further provided in § 4.05(f) of the Indenture that whenever the amount by which the conversion rate is required to be adjusted is less than one-twentieth of a share of capital stock, Boeing need not make any adjustment. As summarized by the District Court:

" . . . if shares of stock are issued for less than \$50 a share, an adjustment in the conversion rate may be required and that the formula provides for multiplying the number of shares outstanding by

³ "Limited Stock Dividend" is a defined term in the Indenture. See Ex. 4 to ASOF at § 1.01 p. 17.

\$100 and dividing such figure by the total consideration received for all shares; if the quotient obtained is more than 2.05, an adjustment in the conversion rate is required." (290a-291a).

From March 10, 1961, until the debentures were redeemed on April 8, 1966, Boeing treated the conversion rate as 2.0448. Plaintiffs contend that the proper rate should have been 2.0725 or more, which would have necessitated the issuance by Boeing of additional shares of capital stock upon plaintiffs' conversion of their debentures (304a; Winer Brief at 50-51).

C. The Redemption

The debentures were subject to redemption on terms and conditions set forth in the debenture (Ex. 1 to ASOF) and the Indenture (Ex. 4 to ASOF), which were the only contractual arrangements between Boeing and the plaintiffs. The Indenture provided in pertinent part with respect to a call of the debentures for redemption that Boeing

"... shall publish prior to the date fixed for redemption a notice of such redemption at least twice in an Authorized Newspaper,⁴ the first such publication to be not less than 30 days and not more than 90 days before the date fixed for redemption. Such publications shall be in successive weeks but on any day of the week. It shall not be necessary for more than one such publication to be made in the same newspaper." (Ex. 4 to ASOF at § 5.02).

⁴ "Authorized Newspaper" is defined in the Indenture as a newspaper of general circulation, published at least five days a week in the Borough of Manhattan. See Ex. 4 to ASOF at § 1.01 p. 10. See also, District Court's Opinion at 297a.

On February 28, 1966, Boeing's Board of Directors authorized the officers of the Company to redeem the debentures as part of a substantial financing program incident to the development of Boeing's jet aircraft and supersonic transport programs (292a-294a).

Between March 2-7, 1966, Boeing representatives and others tentatively agreed that the redemption date for the debentures would be April 8, 1966. By March 7th it was determined by Boeing that notice of redemption of the debentures as provided in § 5.02 of the Indenture would be published in all regional editions of The Wall Street Journal (not just in the Eastern edition which would have satisfied the Indenture) on March 8 and 18, 1966 (295a). Thereafter, Boeing published notice of the redemption in excess of the requirements of the Indenture in all editions of The Wall Street Journal on March 8, 18 and 28, 1966, and in The New York Times on March 28, 1966, in the form set forth below (Exs. 46 and 51 to ASOF):

The Boeing Company

(formerly Boeing Airplane Company)

Notice of Redemption of 4½ % Convertible Subordinated Debentures, due July 1, 1980

NOTICE IS HEREBY GIVEN that, pursuant to the provisions of the Indenture dated July 1, 1958, between Boeing Airplane Company (now The Boeing Company) (hereinafter called the Company) and The Chase Manhattan Bank (now The Chase Manhattan Bank [National Association]), Trustee, the Company has exercised its option to and will redeem, on April 8, 1966, all of its outstanding 4½ % Convertible Subordinated Debentures, due July 1, 1980 (hereinafter called the Debentures), at the redemption price of 103.25% of the principal amount thereof, together with accrued interest to said redemption date.

On and after April 8, 1966, interest on the Debentures shall cease to accrue and the coupons for interest maturing after said date shall be void.

Payment of the redemption price, with accrued interest to the date fixed for redemption, will be made at the principal office of the Trustee upon presentation and surrender for redemption, on or after April 8, 1966, of the Debentures with all coupons appertaining thereto, if any, maturing after the date fixed for redemption. Coupons maturing prior to the redemption date should be detached and surrendered for payment in the usual manner. The Debentures should be presented at The Chase Manhattan Bank N. A. (Corporate Agency Department), 80 Pine Street, New York, New York 10015.

CONVERSION RIGHT

Subject to the provisions of the Indenture, the holder of a Debenture is entitled at his option to convert such Debenture, or any portion thereof which is \$100 principal amount or a multiple thereof, into shares of Capital Stock of the Company. This right of conversion will terminate at the close of business on March 29, 1966. The conversion rate now in effect is 2 shares of Capital Stock for each \$100 principal amount of Debentures. As provided in the Indenture, no adjustment shall be made for interest accrued on any Debenture surrendered for conversion or for dividends on shares of Capital Stock issuable upon conversion of any Debenture.

From January 1, 1965 through March 3, 1966, the sales price for the Common Stock of the Company on the New York Stock Exchange ranged from a high of \$175.25 to a low of \$60.375 per share. On March 3, 1966, the last sale of such Common Stock on such Stock Exchange was at \$158.25 per share. So long as the market price of Common Stock is \$52.24 or more per share, a Debentureholder would receive, upon conversion of Debentures, Common Stock having a greater market value than the cash which such holder would receive if he surrendered Debentures for redemption.

The Boeing Company

By DEAN D. THORNTON, Treasurer

Dated: March 8, 1966

Boeing also gave the requisite notices to the NYSE and others and took additional steps necessary to effect the redemption, including sending notices by letter to all registered debenture holders and holders of bearer debentures registered as to principal at their registered addresses (295a-298a).

As of March, 1966, the market price for Boeing capital stock was in excess of the redemption price and, accordingly, it was advantageous to debenture holders to convert their debentures into Boeing stock prior to the expiration of the conversion privilege on March 29, 1966, rather than to redeem. For this reason it was of particular significance that the paid, printed notice published by Boeing contained the statement to which the arrow (">") above points:

"This right of conversion will terminate at the close of business on March 29, 1966."

While the vast majority of debenture holders (92.8% of the \$21,514,000 outstanding face amount of debentures on March 8, 1966) did exercise their conversion rights in a timely manner, the plaintiffs (7.2% or \$1,544,300 of the aggregate outstanding face amount) failed to do so (298a). Boeing considered the possibility of extending the conversion deadline but on the advice of its counsel that it had no power or right under the Indenture or otherwise to do so, it refused to allow any of the plaintiffs to effect untimely conversions (298a).⁵

⁵ See opinion letter of Holman, Marion, Perkins, Coie & Stone to Boeing dated April 25, 1966, and opinion letter of Davis Polk Wardwell Sunderland & Kiendl to Boeing dated April 27, 1966 (137a-141a). Extension of the conversion deadline could have been challenged as a waste of corporate assets and, in any event, would have been in violation of the fiduciary duty owed by the Board of Directors to Boeing's stockholders.

ARGUMENT

I

THE DISTRICT COURT CORRECTLY HELD THAT NOTICE OF THE CALL OF THE DEBENTURES WAS "REASONABLE, VALID AND ADEQUATE"

The District Court's conclusion of law that Boeing "was bound to give only such notice as was spelled out in the Indenture and in the Debenture, which incorporated the Indenture" (300a) accords not only with all cases of which we are aware that have considered the issue, but also with the statutory purpose of the Trust Indenture Act of 1939, 15 U.S.C. § 77aaa *et seq.* (the "1939 Act"). The District Court quite properly rejected plaintiffs' claim, which they again make here, that Boeing was obliged to give its debenture holders notice which met their "reasonable expectations" even if such notice be in excess of that provided in the Indenture because it was a "contract of adhesion" (299a; Winer Brief at 67-68).

Despite extensive argument, plaintiffs have said nothing in their briefs which, in any way, undermines the validity of the District Court's holding that:

"The notice required was not only adequate, but the defendants did more than was required when they published a third time on March 28, 1966 in all editions of the Wall Street Journal and in the New York Times, with the 'dramatic and widespread rippling effect'⁶ which brought in over \$9,000,000

⁶ The District Court found as a fact:

"Notices of the dates of the call and the expiration of the conversion privilege on March 29, 1966 were carried on the following services: NYSE ticker on March 8, 23, 24, 25, 26 and 28, 1966; NYSE Bulletin on March 11, 18 and 25, 1966; The Commercial and Financial Chronicle on March 14, 21

face amount of debentures for redemption. In fact, the very minimal aggregate number of non-converting debenture holders, which constitute the class represented, speaks eloquently for the adequacy of notice given by defendants." (300a).

The cases make it clear beyond peradventure that the result reached by the District Court is eminently correct.

In *Abramson v. Burroughs Corp.*, CCH Fed. Sec. L. Rep. [1971-1972 Transfer Binder] ¶ 93,456 (S.D.N.Y. 1972), Judge Lumbard (sitting by designation as a District Judge) held that:

"In the context of the organized financial markets, with their centers in New York City, Burroughs was reasonable in assuming that notice published in New York in the New York Times and the Wall Street Journal was best calculated to come to the attention of Burroughs bondholders. Even if the bondholders themselves did not receive the notice, their brokers were certain to receive it and Burroughs was reasonable in believing that any broker who received notice of the Burroughs redemption would in turn notify his clients who held Burroughs convertible bonds." At p. 92,254.

Virtually on all fours with this case on the question of the adequacy of the notice provided for in the Indenture

and 28, 1966; Standard & Poor's Bond Outlook on March 19, 1966; Standard & Poor's Called Bond Record on March 9, 11, 18 and 25, 1966; Moody's Industrial's on March 11, 1966. Articles about these dates were carried in the Seattle Post Intelligencer on March 25, 1966; the Seattle Times on March 27, 1966; and the Financial World on March 23, 1966. The notice also was carried in the Associated Press Bond Tables published on one or more days in at least 30 newspapers published in major cities across the United States." (297a).

and which Boeing gave is *Kaplan v. Vornado, Inc.*, 341 F. Supp. 212 (N.D. Ill. 1971). There, as noted by the Court below:

"[T]he Court held that the debenture holder was bound by the terms of the Indenture, which he did not see, as well as by the terms of the Debenture, which he did not understand; and that the notice was sufficient, even though it was published in a New York newspaper and various publications which plaintiff, a resident of Kansas, never saw." (302a).

As to the adequacy of the published notice provided for in the indenture and given pursuant thereto by Vornado, the Court in that case held as follows:

"In beginning it may be noted that the holders of these debentures had the option of registering with the trustee and receiving personal notice. Plaintiff also failed to take this step. This practice of registration has been suggested as a solution to the problem of security holders not receiving notice by publication. Note, *Convertible Securities*, supra. As far as publishing in the N.Y. Times, plaintiff [sic] made every reasonable effort to publicize its decision as evidenced by the number of papers which carried the story. It has always been recognized that notice by publication will not reach all of its intended recipients but plaintiff could have avoided this result by registering.

* * *

The court is of the opinion that, when considered in conjunction with plaintiff's right to register, the notice published by defendant was reasonable. . . ." 341 F. Supp. at 216-17.

See also *Kraus v. Laclede Gas Co.*, 354 S.W.2d 327 (St. Louis Ct. App. 1962); *Gampel v. Burlington Industries, Inc.*, 43 Misc. 2d 846, 252 N.Y.S.2d 500 (Sup. Ct. N.Y. County 1964); *Mueller v. Howard Aircraft Corp.*, 329 Ill. App. 570, 70 N.E.2d 203 (1946).

In *Gampel v. Burlington Industries, Inc.*, *supra*, the Court considered debenture and indenture notice of redemption provisions quite similar to those at issue here. There, the indenture provided that notice of redemption was to be published once a week for two successive weeks "in one or more newspapers . . . of general circulation in the Borough of Manhattan, City of New York". 43 Misc. 2d at 847, 252 N.Y.S.2d at 501 (emphasis in original). The Court held that the defendant issuer had complied with the notice provision by publishing the notice of redemption in *The Wall Street Journal* because

"... the *Wall Street Journal* is a paper of general circulation and particularly is more widely used than any other paper for the publication of redemption notices." 43 Misc. 2d at 848, 252 N.Y.S.2d at 502.

The law is clear that the Indenture is the sole contract setting forth the rights and duties of Boeing, Chase and the plaintiffs. As the Court stated in *Gampel v. Burlington Industries, Inc.*, *supra*:

"Of course, defendant could have published more than twice and in more than one paper. This was not barred. However, the possible and what is not barred are not the criteria of compliance, but rather whether the minimal possible is compliance." 43 Misc. 2d at 847, 252 N.Y.S.2d at 501 (emphasis added).

Even though Boeing gave more extensive notice of the call of the debentures for redemption than that required by the Indenture and this, as the District Court found, gave rise to a "dramatic and widespread rippling effect" (300a), plaintiffs, nevertheless, claim, as they did at trial, that not even this notice was legally sufficient. *See* Winer Brief at 38-42. The District Court answered this argument of plaintiffs by holding that

"... defendant was bound to give only such notice as was spelled out in the Indenture and in the Debenture, which incorporated the Indenture." (300a).

The Court went on to hold that in light of the fact that bearer debentures such as those at issue here are negotiable upon delivery,

"[t]he suggestions made by plaintiffs as to the further notice which might have been given are not only not required by the terms of the Indenture, but they would have been impracticable, if not impossible." *Id.*

Among plaintiffs' suggestions, obviously without merit because of the freely negotiable nature of bearer securities and quite properly rejected by the District Court, were to send communications to all those who exercised warrants in 1958 when the debentures were issued and to all Boeing stockholders of record at the time of the call. (299a; Winer Brief at 38-40; Kass Goodkind Brief at 59-60). The Court found that "[t]he warrants, as well as the bearer debentures, were traded repeatedly since 1958" and properly concluded as a matter of fact that "it would have been impossible to know in 1966 the names and addresses of the debenture holders." (300a).

As to plaintiffs' contention that Boeing should have ascertained the names and addresses of debenture holders who had presented interest coupons to Chase for payment, the Court ruled as follows:

"Nor would the coupons presented for payment give the names and addresses of the debenture holders. The greater number of these were presented through collecting banks and, although BOEING might have ascertained the owners through the banks, it was under no duty to do so." (301a).

This conclusion was based in part on the Court's finding that

"[a] vast majority of the coupons tendered to the Chase Manhattan Bank came from collecting banks, and Chase Manhattan did not know the identity of the holders of the debentures on whose behalf the coupon tenders were made." (292a).

Plaintiffs have failed to demonstrate that this finding is "clearly erroneous." See *e.g.*, *United States v. General Dynamics Corp.*, 415 U.S. 486, 508 (1974).

In sum, plaintiffs can point to no contractual or statutory obligation imposed on Boeing or to any case which holds that an issuer of bearer debentures is required to give such notice as they urge here as part of a call for redemption of its debentures. Quite obviously, no court has ever imposed such a requirement on any issuer.

Relying to a great extent on a student note, "Convertible Securities: Holder Who Fails to Convert Before Expiration of the Conversion Period," 54 Cornell L. Rev. 271, 272 (1969), plaintiffs contend that because they did not participate in the drafting of the Indenture and form of debenture, that they therefore are parties to a contract of

adhesion that contains an unconscionable notice provision with respect to a redemption of the debentures. *See* Kass Goodkind Brief at 57-58; Winer Brief at 61-68.

It is not disputed by plaintiffs that the debentures were registered under the Securities Act of 1933, 15 U.S.C. § 77a *et seq.* (the "1933 Act") and the Indenture was qualified under the 1939 Act. The 1939 Act was enacted to afford greater protection to investors in corporate debt securities from a number of practices which had been disclosed in reports of the SEC and hearings conducted by Congress. *See* 1939 Act § 302; H.R. Rep. No. 1016, 76th Cong. 1st Sess. at 25 (1939); S. Rep. No. 248, 76th Cong. 1st Sess. at 1-2 (1939). The 1939 Act sets forth a number of "provisions which relate to the protection and enforcement of the rights of the investors" which must be incorporated into an indenture, and if the indenture does not conform to these prescribed statutory standards, the SEC is required to issue an order denying qualification. *See* S. Rep. No. 248, 76th Cong. 1st Sess. at 2 (1939). The Indenture here at issue complies in all respects with the requirements of the 1939 Act and this plaintiffs do not dispute.

It was clearly recognized by the draftsmen of the 1939 Act that because of the nature of the transaction, investors in corporate debentures are not able to participate in the negotiating and drafting of an indenture.

"Where securities are nationally distributed, the investing public cannot participate in the drafting of the indenture or the determination of its terms, because the indenture must be executed before the bonds are issued and before the identity of the ultimate purchasers . . . can be ascertained." *Id.* at 3.

Accordingly, a determination was made that the indenture trustee should act as the guardian and protector of the

debenture holders' rights. Justice William O. Douglas, then a Commissioner of the SEC, made this point quite clearly in the course of testifying on an earlier version of the bill which became the 1939 Act:

"The necessity for reliance of the security holder upon the indenture trustee for protection of his investment is rather complete. It is common knowledge that purchasers of securities, though they are legally bound by the terms of the trust indenture, seldom examine its terms unless they happen to be large and substantial investors." Hearings on S. 2344 before Subcomm. of Senate Comm. on Banking and Currency, 75th Cong. 1st Sess. at 19 (1937).

A convertible subordinated bearer debenture with a call feature is not a necessity of life such as a lease on a home or apartment, a life insurance policy or a contract to purchase a car. *See* Winer Brief at 64-67. Nor are such debentures a common, ordinary type of investment. The plaintiffs, investors in a sophisticated form of corporate security, convertible subordinated bearer debentures with a call provision, should have been aware of the nature of their investment, the circumstances and practices of the debenture market and, of course, the risks involved in making such an investment.

The Official Comment to Uniform Commercial Code § 2-302, "Unconscionable Contract or Clause", states that the basic test with respect to unconscionability

"... is whether, in the light of the general commercial background and the commercial needs of the particular trade or case, the clauses involved are so one-sided as to be unconscionable under the circumstances existing at the time of the making

of the contract. * * * The principle is one of the prevention of oppression and unfair surprise . . . and not the disturbance of allocation of risks because of superior bargaining power." (McKinney's 1964).⁷

Clearly under this test, § 5.02 of the Indenture is valid and enforceable in accordance with its terms and the District Court correctly so held (300a-303a).

A substantial risk assumed by any investor who selects convertible bearer debentures with a call feature is that they will be called for redemption and that he may not learn of the call until after the expiration of the conversion privilege. Bearer debentures are negotiable by delivery as was clearly stated on the face of the debentures here at issue (Ex. 1 to ASOF). The District Court found that "the warrants, as well as the bearer debentures, were traded repeatedly since 1958, so that it would have been impossible to know in 1966 the names and addresses of the debenture holders" (300a). It was this freely negotiable nature of bearer securities that made them an attractive medium for investment despite the possible attendant risks of not receiving notice of a call for redemption. *See generally*, Sebring, "The Coupon Bond: A Costly Paradox," 17 Bus. Law. 844 (1962); Sebring, "The Coupon Bond: A Costly Paradox—A Postscript," 18 Bus. Law. 429 (1963).

The District Court found as a fact that it "was stated twice on the face of the debenture, as well as several places

⁷ For the application by analogy of the sale of goods sections of UCC (Art. 2) to investment securities (Art. 8) *see, e.g.*, Official Comment to Uniform Commercial Code § 2-105 at 96-97; *Hunt Foods & Industries, Inc. v. Doliner*, 49 Misc. 2d 246 (Sup. Ct. N.Y. County), *rev'd on other grounds*, 26 A.D.2d 41 (1st Dep't 1966).

in the Indenture" that the debentures could be registered (287a). The Court then concluded as follows:

"Plaintiffs held the debentures which clearly stated that they could be registered; plaintiffs could have done so and they would have been notified by mail of the call thus eliminating the real risk of not seeing the notices and press releases. Plaintiffs chose not to do so, and they must bear the consequences (*Kraus v. Laclede Gas Co.*, 354 S.W.2d 327 (St. Louis Ct. of App. 1962))." (303a).

Quite obviously, plaintiffs, who not only failed to take the simple, reasonable step of registering their debentures, but who also negligently failed themselves or through an agent to watch for the call of the debentures for redemption cannot now obtain a belated benefit at the cost of Boeing and its stockholders. In accord with the District Court's opinion on this point is *Abramson v. Burroughs Corp.*, CCH Fed. Sec. L. Rep. [1971-1972 Transfer Binder] ¶ 93,456 (S.D.N.Y. 1972), which involved a claim by a holder of bearer convertible debentures who failed to learn of a call of his debentures until after the conversion privilege had terminated. There the Court held that "[h]is [the plaintiff's] failure to register the bonds (or otherwise assure himself of notice) was his fault, not Burroughs." *Id.* at p. 92,254.

To the same effect is *Kaplan v. Vornado, Inc.*, 341 F. Supp. 212, 215-16 (N.D. Ill. 1971):

"It does not seem to be unreasonable to expect an investor, who is unfamiliar with debentures, to at least read the terms on the face of the debenture in more detail than the general information at the top of the debenture. Small printing may always be

something of a deterrence to its being read but an investor cannot reasonably rest upon his lack of knowledge and fail either to read the debenture or seek information concerning its important terms from a knowledgeable source. It was due to these failures that plaintiff was caught unaware when the defendant redeemed the debenture. Lack of knowledge combined with a refusal to exercise due care in protecting one's interest does not state a claim for relief even under 10b-5. Under these circumstances, it is most probable that had the alleged nondisclosure not occurred, plaintiff would not have acted in a different manner.

If plaintiff had taken any of these steps, he would have been aware of the redemption rights of defendant and might have avoided his loss.

* * *

In the case at bar, a reasonable investor would have at least made inquiries concerning the terms of the debentures even if he didn't read all of the small print and didn't know what the terms of the debenture were, and there was a good reason for the differences of the type. One portion was the title of the debenture while the remainder consisted of the entire body of terms governing the relationship between the parties (except for the provisions of the Indenture Agreement which were incorporated by reference)."

In 1958, at the time of the issuance of the debentures by Boeing and the execution of the Indenture with Chase acting as trustee on behalf of all present and future debenture holders including the plaintiffs, the risk that actual notice

might not be received by subsequent holders of the debentures was clearly accepted by all even remotely familiar with the nature of such debentures. It was just such a risk which led Boeing to accord purchasers the option of registering their debentures either fully or as to principal. Such an option was again widely accepted in the trade and often exercised by investors purchasing convertible debentures. With respect to bearer debentures, notice by publication as provided for by the Indenture was standard and conformed with the custom and practice prevailing in the trade in 1958. *See generally, Gampel v. Burlington Industries, Inc.*, 43 Misc. 2d 846, 252 N.Y.S.2d 500 (Sup. Ct. N.Y. County 1964); *Abramson v. Burroughs Corp.*, *supra*; Note, "Convertible Securities: Holder Who Fails to Convert Before Expiration of the Conversion Period," 54 Cornell L. Rev. 271, 278 (1969); American Bar Foundation Corporate Debt Financing Project, Model Debenture Indenture Provisions § 1105 (1965); R. McClelland & F. Fisher, Jr., *Law of Corporate Mortgage Bond Issues* 543 (1937).

As the District Court noted in its opinion, any investor who purchased these Boeing debentures, including the plaintiffs, who was concerned about receiving notice of a call had several alternatives open to him (287a-303a). He could have purchased his debentures in fully registered form thus insuring that notice of a call would be sent to him at his registered address (Ex. 4 to ASOF at §§ 2.03 and 5.02). Further, as stated on the face of the debentures and pursuant to §2.06 of the Indenture, bearer debentures could be registered as to principal. If this were done, §5.02 of the Indenture provides that notice of any call would be sent to the registered holder at his registered address.

None of the plaintiffs in this case, for reasons known only to them, chose to register their debentures. Failing to

take advantage of the simple registration option, which as the District Court noted "was stated twice on the face of the debenture, as well as in several places in the Indenture" (287a), and which could have been availed of without charge (Ex. 4 to ASOF at § 2.06), plaintiffs still could have protected their conversion right by making arrangements to have a bank, broker, investment advisor or some other third party watch for a redemption notice if they themselves did not wish to have to be concerned with the matter.

Here, as in the District Court, plaintiffs have based their argument with respect to the alleged inadequacy of the notice of the call given by Boeing almost entirely upon cases dealing with the notice constitutionally required to be given to interested parties in judicial proceedings where, unlike here, there was no specific contract between the parties setting forth the procedures for notice. See Winer Brief at 68-70; Kass Goodkind Brief at 59. The District Court clearly recognized that the cases cited by plaintiffs there and here are inapposite:

"*Mullane v. Central Hanover Trust Co.*, 339 U.S. 306 (1950) and the other cases relied on by plaintiffs are not relevant in that, in those cases, the Courts struck a notice by publication as insufficient to bar a party in a judicial proceeding where another kind of notice was possible. *Walker v. Hutchinson*, 352 U.S. 112 (1956) condemnation proceedings; *New York v. N.Y. Central R.R. Co.*, 344 U.S. 293 (1953) wiping out a tax lien in a bankruptcy proceeding" (302a).

Plaintiffs place great emphasis on *Mullane v. Central Hanover Bank & Trust Co.*, *supra*, in support of their argument that the notice provided for in § 5.02 of the Indenture is legally defective. In *Mullane*, the Central Hanover Bank,

acting as trustee of a common trust fund, sought to settle certain accounts by publishing notice to the beneficiaries in strict compliance with the minimum requirements of the New York Banking Law. The names and addresses of some of the beneficiaries were known to the Bank and in fact they had received personal notice by mail at the time the common trust fund had been established. *Id.* at 319. The Supreme Court held that there was no violation of due process with respect to the statutory notice by publication given to those beneficiaries whose interests or addresses were unknown to the trustee because there was no other means of giving them notice which was both practical and more effective. It did hold such notice to be constitutionally impermissible as to those beneficiaries whose names and addresses were known to the trustee. Here the names and addresses of the plaintiffs were unknown to Boeing because plaintiffs were holders of bearer debentures negotiable by delivery. Thus the notice by publication provided for in § 5.02 of the Indenture is consistent with *Mullane*, assuming that the case were extended from notice provided by statute for a judicial proceeding to notice provided by contract, an extension which, to our knowledge, has never been made. *Accord, Schroeder v. New York*, 371 U.S. 208, 212-13 (1962).

The District Court properly rejected plaintiffs' argument, which they again advance here, that Boeing violated §§ 8.01 and 8.02 of the Indenture and § 312(a) of the 1939 Act by not furnishing to Chase at least every six months the names and addresses of additional debenture holders who became known to Boeing and its paying agent (other than Chase) (303a; Winer Brief at 72-73). The Court made a factual finding that "[f]rom 1959 to 1966, no such information came to the knowledge of BOEING and it gave none to the Trustee." (292a). Plaintiffs assert that "the Trust Indenture Act was cavalierly disregarded" (Winer Brief at 73) but have failed completely to make any show-

ing as why the Court's finding on this point is "clearly erroneous." As the District Court held: "The answer to this is that it was stipulated that BOEING had no names to furnish Chase Manhattan and so advised it under the terms of the Indenture." (303a).

Absolutely lacking in merit is the claim advanced by plaintiffs for the first time on appeal that the notice of the call given by Boeing was so defective as to constitute a violation of Section 10(b) of the 1934 Act (Winer Brief at 71-72). The District Court's conclusion that "[t]he notice required was not only adequate, but the defendants did more than was required" (300a) accords with the decisions of all other courts that have been faced with such an issue. See, e.g., *Abramson v. Burroughs Corp.*, CCH Fed. Sec. L. Rep. [1971-1972 Transfer Binder] ¶ 93,456 (S.D.N.Y. 1972); *Kaplan v. Vornado, Inc.*, 341 F. Supp. 212 (N.D. Ill. 1971).

Plaintiffs' reliance on an SEC Staff Letter sent in response to an inquiry from one Karl E. Sommerlatte as to whether the SEC has rules requiring notification to debenture holders of redemptions of convertible debentures does nothing to impugn the validity of the District Court's holding (Winer Brief at 71-72). Sommerlatte wanted to know if the SEC had such rules and if so whether they permit notice by publication. CCH Fed. Sec. L. Rep. [1970-1971 Transfer Binder] ¶ 75,557 (November 8, 1971). In reply the SEC said that there were no provisions of the federal securities laws with respect to this issue but that there might be situations where "the antifraud provisions of the federal securities laws *may be applicable*." *Id.* at p. 81,202 (emphasis added). We certainly do not take issue with this statement of the SEC's position but quite obviously it has no bearing on the adequacy of notice question that was decided by the District Court.

In sum, as the District Court held, "the notice of call was reasonable, valid and adequate." (303a). There is absolutely no support in the record or in the applicable cases for the position advanced by plaintiffs to this Court as to the validity of the notice given to the call of the debentures for redemption.

II

THE DISTRICT COURT CORRECTLY CONCLUDED THAT "NEITHER THE 4% NOR THE 2% LIMITED STOCK DIVIDEND, NOR THE ACQUISITION OF VERTOL, NOR ANY COMBINATION OF THESE THREE EVENTS, REQUIRED AN ADJUSTMENT OF THE CONVERSION RATE"

A. There Is No Basis In Law Or Fact For Disturbing The District Court's Determination That Boeing Correctly Applied The Clear And Unambiguous Provisions Of The Indenture With Respect To The Consideration Deemed To Have Been Received Upon Declaration Of The 4% And 2% Limited Stock Dividends

The only issue at trial with respect to the Limited Stock Dividends was whether Boeing correctly applied the formula set forth in § 4.05 of the Indenture, which provides in relevant part:

"(b) For the purpose of this Section 4.05, the Company shall be deemed to have received as consideration for the shares of its Capital Stock outstanding at the time of making any computation hereunder the sum of \$351,872,350 plus any additional consideration received by the Company after July 1, 1958, which consideration shall be determined as follows:

* * * *

(iv) In the case of shares issued as a Limited Stock Dividend the consideration shall be deemed to be *the number of shares so issued multiplied by the market value thereof (determined as provided in the definition of 'Limited Stock Dividend' in Section 1.01) on the date of the declaration thereof; . . .*" (Ex. 4 to ASOF; emphasis added).

The "market value thereof" is defined in unmistakably clear language in § 1.01 of the Indenture under the heading "Limited Stock Dividend":

"For the purposes of this definition market value shall mean *the last reported sale price . . . on the date of declaration of each stock dividend. . . .*" (Emphasis added).

With respect to the 4% Limited Stock Dividend declared on November 3, 1958, the Court held that Boeing correctly applied this formula by multiplying \$56.875—the last reported sales price of Boeing capital stock on the NYSE on that day—times 281,537—the number of shares issued under the 4% Limited Stock Dividend—which resulted in a figure of \$16,012,417 as the total consideration paid for the shares issued (305a-306a). The Court similarly held that Boeing properly applied the Indenture formula to the 2% Limited Stock Dividend declared on November 2, 1959. With the 2% Limited Stock Dividend Boeing took the number of shares of its capital stock issued for the dividend declared that day (147,489) and multiplied it by the closing price on the NYSE of \$30.375 for a total consideration of \$4,479,979 (305a-306a).

Plaintiffs contend here, as they did at trial, that the definition of "market value" in § 1.01 of the Indenture should be rewritten by the Court to add language to the effect that "market value will be computed by dividing by 100 plus the percentage points of the Limited Stock Dividend," i.e., 102 in the case of the 2% Limited Stock Dividend and 104 in the case of the 4% Limited Stock Dividend. (307a; Winer Brief at 47-50). The short and complete answer to this contention and that given by the District Court is that this simply is not what the Indenture provides:

"The terms of the Indenture are clear in that the market value of a limited stock dividend is defined as the last reported sales price on the date of the declaration of the dividend (Section 1.01). Plaintiffs would construe this to mean that this includes the sales price including the additional shares issued as a result of the dividend, or post dividend rather than ex-dividend, arguing that this is the more intelligent meaning because it represents more accurately the market value of the shares. This may be so but the Indenture was drawn by BOEING, how to define market value was its decision to make out of several alternatives. BOEING had a right to so define it, and, having done so, it had not only the right but the duty to comply with the definition set forth in the Indenture, irrespective of its motive." (307a).

The Court quite properly gave little if any weight to the fact that Boeing's "original computation of the 4% Limited stock dividend was not proper under the terms of the Indenture. . . ." (307a). The Court correctly observed, as was made "according to the usual corporate accounting the testimony indicated,"⁸ that this erroneous computation practice" and not in accordance with the Indenture formula (307a).

The provisions of the Indenture are clear and unambiguous and the District Court correctly held that Boeing had no power to compute the conversion rate in contravention of the formula set forth in the Indenture. To do so in this case would have resulted in a gift to the debenture holders and thus have been a clear violation of the Board of Direc-

⁸ See testimony of Gerald E. Gorans, a partner of Touche, Ross, Bailey & Smart, Boeing's independent auditors (627a-629a), and of Harold F. Olsen, Boeing's outside general counsel (569a-574a).

tors' fiduciary duty to the stockholders of Boeing. *Frankel v. Donovan*, 35 Del. Ch. 443, 120 A.2d 311 (1956); *J. & R. A. Savageau, Inc. v. Larsen*, 118 Colo. 142, 193 P.2d 1005 (1948).

B. The District Court's Determination That Boeing's Board Of Directors Acted In Good Faith In Fixing The Fair Value Of The Assets Of Vertol Is Fully Supported By The Evidence

Plaintiffs' multi-faceted arguments on the Vertol valuation issue (Winer Brief at 13-18; 42-58) must fail because plaintiffs have not been able to show that the District Court's factual finding of good faith is "clearly erroneous." See, e.g., *Zenith Radio Corp. v. Hazeltine Research, Inc.*, 395 U.S. 100, 123 (1969). This is particularly true where the Court's finding is based upon oral testimony and the trial judge has viewed the credibility and demeanor of witnesses. See generally, 9 C. Wright & A. Miller, *Federal Practice & Procedure: Civil* § 2585 (1971).⁹

Section 4.05 (b) (ii) of the Indenture provides that "[i]n the case of the issuance of shares for a consideration in whole or in part other than cash, the consideration other than cash shall be deemed to be the fair value thereof as determined by the Board of Directors;" (Ex. 4 to ASOF; emphasis added). Such a determination was made by the Boeing Board of Directors on April 4, 1960 (Ex. 25 to ASOF). At this meeting it was determined that the "fair

⁹ Here the District Court heard testimony with respect to this issue by William M. Allen, former President of Boeing (361a-372a; 395a-412a; 424a-427a); Harold W. Haynes, Senior Vice President of Finance of Boeing (475a-487a); Harold F. Olsen, a member of the law firm now known as Perkins, Coie, Stone, Olsen & Williams, which acts as general counsel for Boeing (561a-563a); Gerald E. Gorans, a partner of Touche, Ross, Bailey & Smart, Boeing's independent auditors (625a-627a; 646a-676a) and from plaintiffs' expert accounting witness, Samuel Pivar of Seidman & Seidman (598a-613a).

value" of the consideration paid to Vertol was to be determined on the basis of the market value of the 448,954 shares of Boeing capital stock on November 13, 1959 (\$15,250,000), plus the \$644,514 to be received upon the exercise of Vertol stock options, for a total of \$15,894,514 (ASOF ¶ 77 at 184a).¹⁰

With respect to this determination by Boeing's Board of Directors, the District Court observed:

"[T]his Court cannot say that the Board of Directors had no colorable right to fix the 'fair value' of the consideration as of November 13, 1959. The decision was carefully taken not only with the approval of its accountants but of independent auditors, outside counsel, its investment bankers and underwriters, with the unanimous resolution of its Board and in good faith. This is the test rather than whether another method of valuation might seem more appropriate. * * * There is ample authority to support a decision made by a Board of Directors under similar conditions; in fact *it is conclusive*." (311a; emphasis added).

Plaintiffs contend here, as they did at trial, that this determination by Boeing's Board of Directors should be upset because the Board should have used the price of Boeing capital stock on March 31, 1960, the date of closing of the contract, or the price of Boeing capital stock on the date the contract was signed, January 18, 1960, either of which

¹⁰ On November 13, 1959, Boeing's Directors made the decision that the Company should commence negotiations to acquire substantially all of the assets of Vertol in exchange for 448,954 shares of capital stock of Boeing, plus an agreement to issue 23,782 additional shares of stock of Boeing upon the exercise of options held by Vertol employees to purchase Vertol stock. Representatives of the two companies proceeded promptly to work out all of the details and the transaction was completed on March 31, 1960. (309a-310a).

alternatives would have resulted in a lower valuation of Vertol and have triggered an adjustment in the conversion rate (308a; Winer Brief at *e.g.* 35).

The law is clear, as the District Court held, that directors of a corporation have very broad discretionary power in valuing assets for particular purposes and courts are extremely reluctant to override the exercise of their business judgment. In *Randall v. Bailey*, 23 N.Y.S.2d 173 (Sup. Ct. N.Y. County 1940), *aff'd*, 262 App. Div. 844, 29 N.Y.S.2d 512 (1st Dep't 1941), *aff'd* 288 N.Y. 28, 43 N.E.2d 43 (1942), (valuing assets for purposes of dividend declarations), it was said:

"What directors must do is to exercise an informed judgment of their own, and the amount of information which they should obtain, and the sources from which they should obtain it, will of course depend upon the circumstances of each particular case. * * * When directors have in fact exercised an informed judgment with respect to the value of the company's assets, the courts obviously will be exceedingly slow to override that judgment, and clear and convincing evidence will be required to justify a finding that such judgment was not in accordance with the facts." 23 N.Y.S.2d at 184-85.

To the same effect, see *Morris v. Standard Gas & Electric Co.*, 31 Del. Ch. 20, 63 A.2d 577, 585 (1949), in which the Court said:

". . . I am persuaded that this court can not substitute either plaintiff's or its own opinion of value for that reached by the directors where there is no charge of fraud or bad faith. As stated, the process of valuation called for by Section 34(b) [of the Delaware General Corporation Law] of necessity

permits of no one objective standard of value. Having in mind its function, the directors must be given reasonable latitude in ascertaining value. Such being the case, I conclude that the action of the directors . . . cannot be disturbed on the showing here made."

Accord, Clinton Mining and Mineral Co. v. Jamison, 256 F. 577 (3d Cir. 1919), *cert. denied*, 254 U.S. 637 (1920). See also, 11 *Fletcher, Corporations* §§ 5221, 5336 and 5344 (1971).

Industrial & General Trust Ltd. v. Tod, 180 N.Y. 215, 73 N.E. 7 (1905), cited by the District Court at 311a, sets out the law of New York, which is applicable to this issue by virtue of the choice of law clause in §17.04 of the Indenture. There the New York Court of Appeals held:

"The power to construe, and the engagement that the construction shall be final mean that it shall be final if the members of the committee act in good faith, but not otherwise. *They were doubtless protected from the outcome of errors of judgment and honest mistakes, but good faith is the standard, erected by the law, by which all their acts and omissions are to be judged.*" 180 N.Y. at 226; 73 N.E. at 9-10 (emphasis added).

The *Tod* case is a leading case in New York and elsewhere and has been frequently cited and followed.

The doctrine that directors have broad discretion in valuing assets for a particular purpose and that their judgment can be overturned only upon a showing of bad faith is particularly applicable here where the Directors relied on the opinions of Boeing's investment banking advisors (Harri-

man Ripley & Co.), outside legal counsel (Harold F. Olsen of Perkins, Coie, Stone, Olsen & Williams), and a firm of independent auditors (Touche, Ross, Bailey & Smart) in addition to a report from a qualified financial expert within the Boeing organization. See District Court's Opinion at 311 (a) ; Ex. 25 to ASOF.

The Delaware Court of Chancery in *Morris v. Standard Gas & Electric Co.*, *supra*,¹¹ indicated that it is the atmosphere in which the directors make their valuation of assets that is crucial. In that case the directors were valuing the assets of their corporation for purposes of determining whether a dividend could be declared. The directors had before them the report of professional appraisers who had been retained to appraise the current value of the assets, a detailed report of their Vice President and Treasurer, who "was eminently qualified in both education and experience to make such an evaluation" (63 A.2d at 580) and the statement of the Chairman that he had examined the reports of the retained appraisers and the Vice President, that he agreed with their conclusions, and explaining the methods he used in his study and evaluation. The opinions of two Delaware attorneys and one Chicago attorney as to the legality of the proposed dividend were read to the meeting. On these facts the Court accepted the valuation placed on the property by the directors.

See also, *Gilbert v. Burnside*, 13 App. Div. 2d 982, 983, 216 N.Y.S.2d 430, 432 (2d Dep't 1961), to the effect that a board of directors' "[r]eliance upon advice of counsel is a good defense (*Blaustein v. Pan Amer. Petroleum & Transp. Co.*, 293 N.Y. 281)."

Plaintiffs' claim that the Vertol valuation is tainted by the Board's alleged conflict of interest is wholly lacking in

¹¹ Cited with approval by the District Court at 311a.

merit (Winer Brief at 22-23). As the District Court noted:

"Plaintiffs admit that the formula provided for in the Indenture had as its purpose the prevention of dilution of stock to the detriment of BOEING stockholders. It was certainly BOEING's duty and right to compute stock in such a way as to prevent its dilution and there is no evidence that it had any purpose of deliberately hurting its debenture holders." (310a-311a).

The Board of Directors owed a fiduciary duty to Boeing stockholders to protect their investment. It also owed a duty to the debenture holders to act in good faith. The fact that a decision made by the Board in good faith, as the District Court held, might prove to be more advantageous to the stockholders than other possible decisions it might have made is of no consequence.

Plaintiffs do not challenge the District Court's approval of the "barter-equation" method of valuation used by Boeing's Board, *i.e.*, valuing Vertol on the basis of the value of Boeing capital stock which Boeing was prepared to exchange for Vertol's assets.¹² What plaintiffs do dispute is the District Court's refusal to overturn the use by the Boeing Board of November 13, 1959, as the date to fix the "fair value" of the consideration paid for Vertol's assets (Winer Brief at 35, 44-47).

The cases cited by plaintiffs are wholly inapposite as they deal either with § 16(b) of the 1934 Act or the Internal Revenue Code, both of which statutes reflect unequivocal

¹² In any event, such a contention would be fruitless as this method has received increasing judicial approval. See *Seas Shipping Co. v. C.I.R.*, 371 F.2d 528 (2d Cir.), *cert. denied*, 387 U.S. 943 (1967); *Southern Natural Gas Co. v. United States*, 412 F.2d 1222 (Ct.Cl. 1960); *Bar L Ranch, Inc. v. Phinney*, 426 F.2d 995 (5th Cir. 1970).

Congressional policies and have absolutely nothing to do with the valuation determination Boeing's Board made on April 4, 1960, pursuant to § 4.05 (b) (ii) of the Indenture (Winer Brief at 46-47).

Plaintiffs have pointed to no case which could, by any stretch of the imagination, be considered authority for this Court's overturning the trial court's factual determination that Boeing's Board acted in "good faith" in fixing the "fair value" of the consideration as of November 13, 1959, and its conclusion of law that "[t]his is the test rather than whether another method of valuation might seem more appropriate." (311a). Accordingly, the District Court's ruling that Boeing's valuation of Vertol's assets and business for purposes of the Indenture was wholly consonant with the duty of good faith owed to the debenture holders should not be disturbed.

C. Even Assuming *Arguendo* That An Error Was Made In Fixing The Conversion Rate, The District Court Correctly Held That Plaintiffs Would Have No Standing To Complain

The District Court concluded that "neither the 4% nor the 2% Limited Stock Dividend, nor the acquisition of Vertol, nor any combination of these three events, required an adjustment of the conversion rate." (312a). It further concluded that "even if they had so required it and defendant had failed to do so, plaintiffs who did not convert could not benefit thereby because failure to convert when required to do so would not necessarily have invalidated the call." (*Id.*). These rulings by the District Court are demonstrably correct.

Little need be said about plaintiffs' contention that the Board of Directors' alleged error in setting the conversion

rate was a breach of a condition and the effect was to make the call of the debentures null and void (Winer Brief at 55-61). It is apparent that if any breach occurred, it was totally immaterial and should, at most, give rise to a claim for damages by those persons who did not convert during the specified period. It was in no sense a cause of the plaintiffs' failure to convert. Furthermore, the class consists only of those holders of bearer debentures who failed to convert before the expiration of the conversion privilege on March 20, 1966. See District Court's October 4, 1966, Class Action Order at 83a.

The essence of plaintiffs' complaint in this case is that they were deprived of a right to convert their debentures because they did not receive actual notice of Boeing's decision to redeem. They cannot complain that they were misled by the allegedly erroneous conversion rate published in the notice they contend they did not receive. It is settled law that any such immaterial failure to perform is not a breach of a condition precedent. Restatement of Contracts §§ 274-75 (1932); 6 S. Williston, Contracts § 842 (3d ed. Jaeger 1962); 3A A. Corbin, Contracts §§ 700 *et seq.* (1960); *Jacob & Youngs, Inc. v. Kent*, 230 N.Y. 239, 129 N.E. 889 (1921).

Here, even if there were an error in the published conversion rate, an action for damages would give full compensation to those debenture holders who did convert. However, they are not members of the class and, therefore, are not plaintiffs in this action. Those debenture holders who did not convert could not have been damaged by any such error.

III

THE DISTRICT COURT CORRECTLY HELD THAT "THERE IS NO MERIT OR SUBSTANCE TO PLAINTIFFS' FINAL POINT THAT THE DEFENDANT BOEING BREACHED A CONTRACT IT HAD MADE WITH THE NEW YORK STOCK EXCHANGE"

A. There Is No Basis For Setting Aside The District Court's Factual Finding That "Boeing Did Comply With The Publicity Requirements Of The Exchange"

Plaintiffs claimed at trial, as they do on appeal, that Boeing did not comply with what they consider to be the "publicity requirements" of its Listing Agreement (Ex. 8 to ASOF) as set forth in Section A 10 of the NYSE Company Manual (the "Manual") (Ex. 43 to ASOF) as in effect in 1966 by not issuing a news release when the redemption date was fixed in the first week of March and as a result they have an implied private right of action under the 1934 Act and as third party beneficiaries of the Listing Agreement. *See generally*, Kass Goodkind Brief. The District Court ruled against plaintiffs on both of these issues and expressly found as a matter of fact that "Boeing did comply with the publicity requirements of the Exchange" (312a). This finding was based principally upon the testimony of Boeing's outside counsel, Harold F. Olsen (498a-593a)¹³ and documentary evidence which showed, in the

¹³ The District Court found that:

"By March 7, 1966, the firm dates were fixed as March 8 and 18 to be published in all editions of the Wall Street Journal [sic]. Olsen then called Raftery of the Exchange, informed him of the dates, and requested him to put them on the Dow Jones Tape and the ticker, which Raftery agreed to do. This Olsen, of counsel for BOEING, considered compliance with the publicity requirements of the Exchange (Section A-10 of the New York Stock Exchange Manual)." (295a).

words of the Court, "the dramatic and widespread rippling effect" (300a) of the publicity given the call. *See supra* at 10 n.6.

Despite laborious efforts, plaintiffs have failed to show that this finding of fact is unsupported by the evidence and "clearly erroneous." Plaintiffs attempt to show that Boeing had admitted prior to trial that it did not comply with Section A 10 of the Manual and thus the District Court's finding of fact should be overturned by this Court (Kass Goodkind Brief at 24-28). What Boeing admitted in its Response to Plaintiffs' Request Number 12 for Admissions is that between March 1 and March 24, 1966, it did not issue a general publicity release concerning the call of the debentures (100a). Boeing consistently has taken the position that it complied substantially with Section A 10 of the Manual¹⁴ and there is an unequivocal factual finding that it did (312a). Accordingly, this finding is binding on appeal. *See, e.g., United States v. General Dynamics Corp.*, 415 U.S. 486, 508 (1974).

B. The Manual Is Not And Does Not Purport To Be A Source From Which Implied Causes Of Action May Spring

The District Court correctly held that plaintiffs do not have an implied right of action under the 1934 Act because the Manual is not a "rule" of the NYSE (312a). The Manual is merely a compendium of suggested corporate procedures and guidelines. Moreover, Congress did not intend to create and to our knowledge no court has held that the 1934 Act gives rise to an implied right of action by a security holder against an issuer for the latter's alleged failure to comply with any of the Manual's provisions.

¹⁴ *See, e.g.*, testimony of Harold F. Olsen, Boeing's outside counsel (547a-549a); Defendants' Memorandum Prior to Trial dated May 15, 1972 at 51-54.

When the NYSE has promulgated "rules," it specifically has identified them as such. The three-volume CCH Reporter entitled "New York Stock Exchange Guide" contains one volume devoted to the "Constitution and Rules" of the NYSE. This volume does not include the Manual as a "rule," but rather describes it as "[a] handbook" which "outlines good corporate practice." 1 New York Stock Exchange Guide at 937. The Manual itself refers to some NYSE rules (*See, e.g.*, Manual Section A 8—"Proxies—Meetings of Stockholders"), but these references simply reinforce the point that the Manual itself is not a book of "rules," but rather is, as it purports to be, a guide or handbook setting forth suggested procedures.

Not only is the Manual not identified by the NYSE as a "rule," nor included in the CCH compilation as a "rule," but there is nothing in the Listing Agreement—the sole contract between the NYSE and each listed company—which incorporates the Manual as part of that agreement or refers to it in any way. *See* Boeing Listing Agreement, Ex. 8 to ASOF.

The question of what is a NYSE "rule" was before Judge Frankel in *DeRenzis v. Levy*, 297 F. Supp. 998 (S.D.N.Y. 1969), a case which was cited by the Court below (313a). In *DeRenzis* plaintiff asserted a claim against a NYSE member based on violation of a directive contained in certain "Supplementary Material" within the CCH volume devoted to the NYSE's Constitution and Rules. Judge Frankel noted the provision's "far physical remove, . . . from the nearest preceding pronouncement labelled a 'rule,'" and undertook the following careful analysis:

"All this about typography, locus in a book, and numeration has, to be sure, a paltry and unedifying sound. At least it seemed so on first hearing to one

listener. A little reflection, however, makes a difference. In addition to its more inspiring qualities and prior to them, the 'law' should be as visible, identifiable, and certain as we can contrive to make it. * * * Assuming plaintiff's answer to the hard question whether stock exchange rules may ever give rise to rights like that asserted here, this could only be true if, at a minimum, the propositions in question were promulgated, recorded, and known as rules—or, at least, something closely approximating rules." *Id.* at 1001.

Plaintiffs are unable to point to any statute, regulation or contract to which Boeing was a party that provides that the Manual either is a "rule" of the NYSE or contractually binds a listed company. Quite to the contrary, the Manual is merely a "guide" containing suggested corporate procedures which the NYSE has compiled for listed companies.

The Introduction to the Manual recognizes that the NYSE never intended that the methods and procedures set forth in the Manual be binding requirements.

"In any but the most routine matters, some factors bearing upon the public interest, or the exigencies of the market, may necessitate deviation from even the most explicitly stated policy or requirement, or perhaps introduction of a special measure for a particular case."

Mr. Phillip L. West, who was until recently a Vice President of the NYSE and the head of its Department of Stock List, noted at a panel discussion sponsored by the Practicing Law Institute when questioned about the Manual that:

"There is no specific agreement by the companies that they will abide by these guidelines." A. Fleis-

cher, Jr. and J. Flom, eds., *Texas Gulf Sulphur—Insider Disclosure Problems* 64 (1968).

Furthermore, in *Chris-Craft Industries, Inc. v. Bangor Punta Corp.*, 426 F.2d 569, 576 (2d Cir. 1970), this Court noted that:

“... a policy of the New York Stock Exchange, although entitled to considerable respect, cannot bind the Commission or the Courts.”

Ample support for the District Court's position may be found in the Report of Special Study of Securities Markets of the Securities and Exchange Commission, H.R. Doc. No. 95, 88th Cong. 1st Sess., Pt. 4, Ch. XII at 566 (1963) (the “Special Study”):

“The standards governing conduct of listed companies are found in the listing agreements executed by them and in the company manual published by the Exchange. The company manual is in the nature of a guide for listed companies, and the Exchange expects these companies to comply with its policies. Ultimately the enforcement of the Exchange's requirements flows from the power of the board of governors to suspend and delist securities.”

The Special Study goes on to point out that:

“Most of the problems involving timely disclosure of corporate developments are handled informally by the staff of the Exchange. * * * The ultimate weapon of delisting would be available if a company were habitually to violate the timely disclosure provisions, but the Exchange has never found occasion to go this far.” *Id.* at 567.

As the Special Study states, the NYSE has sufficient authority to punish violations which might defeat the policies

behind the Manual. Cf., *Intercontinental Industries, Inc. v. American Stock Exchange*, 452 F.2d 935 (5th Cir. 1971), cert. denied, 409 U.S. 842 (1972) (delisting permissible where corporation disseminated misleading information concerning corporate developments). Accordingly, even assuming *arguendo* that Boeing violated Section A 10 of the Manual, there is absolutely no basis for implying a private cause of action for violation of disclosure guidelines.

C. No Court Has Ever Implied A Cause Of Action Against An Issuer For Violation Of An Exchange "Rule" Let Alone The Manual

To our knowledge, no cause of action has ever been implied against an *issuer* (as opposed to an *exchange member*) for violation of an exchange "rule." This question was settled ten years ago by this Court in *O'Neill v. Maytag*, 339 F.2d 764 (2d Cir. 1964), which was relied on by the Court below (313a). In *O'Neill* this Court upheld the District Court's refusal to allow plaintiff to amend his complaint to state a cause of action against a listed company under the 1934 Act based upon an allegation that the issuer had violated a NYSE rule. This Court held in no uncertain terms that no cause of action would be implied against the issuer, stating:

"The fourth proposed allegation apparently was intended to establish an entirely new theory by claiming that the transaction violated the rules of the New York Stock Exchange. Whether or not such a violation might give rise to a cause of action against the defendants under state law, we do not think that it does so under federal law. The Exchange itself is under a federal duty to enforce its rules . . . and this duty may be enforceable in a private suit [citations omitted]. . . . It does not

follow, however, that a suit against a listed company or its officers based on violation of an Exchange rule arises under federal law, and we see no reason for so holding." *Id.* at 770.

In view of this holding it is not surprising that plaintiffs cite (and our research has uncovered) not a single case to indicate that the unequivocal rule of *O'Neill v. Maytag* might no longer be the law of this Circuit or for that matter of any other Circuit. While this Court subsequently suggested that there may be instances in which a cause of action for violation of an exchange rule might be implied against a *member* of that exchange, it did not disturb the holding in *O'Neill v. Maytag* with respect to potential liability of an *issuer* of securities listed on an exchange. *Colonial Realty Corp. v. Bache & Co.*, 358 F.2d 178 (2d Cir.), *cert. denied*, 385 U.S. 817 (1966). In *Colonial Realty*, in affirming the dismissal of a cause of action *against an exchange member* based on an alleged violation of a NYSE rule, Judge Friendly described *O'Neill v. Maytag* as "... repudiating a belated attempt to rest federal jurisdiction on a listing agreement between a corporation and the NYSE" and noted that "this court refused to give general recognition to private rights of action for alleged violations of stock exchange rules." *Id.* at 182.

Plaintiffs mistakenly read this language to suggest that *Colonial Realty* overruled the holding in *O'Neill v. Maytag* (Kass Goodkind Brief at 32-33). Certainly, if such a significant result had been this Court's intention, strong words of disapproval of *O'Neill* would have been chosen. The sentence of this Court's *Colonial Realty* opinion which follows its approving citation of *O'Neill v. Maytag* reveals that it intended to draw a distinction between members of an exchange and issuers of securities listed on that exchange. The Court said:

"On the other hand, we cannot ignore that the concept of *supervised self-regulation* is broad enough to encompass a rule which provides what amounts to a substitute for regulation by the SEC itself." 358 F.2d at 182 (emphasis added).

This "supervised self-regulation" of the activities of *members* is required by the 1934 Act itself and the legislative history indicates Congress' intention to regulate exchanges and their members through the system of *self-regulation* to which this Court referred in *Colonial Realty*. See generally, *Silver v. New York Stock Exchange*, 373 U.S. 341, 352 (1962) ; Special Study, Pt. 1, Ch. I at 2-5. At the time the bill embodying what became the 1934 Act was pending, Congress considered extending coverage of the rules and regulations expected to be adopted under the aegis of the 1934 Act to *issuers*, as a condition to having their securities listed on an exchange. See proposed § 12(b) (1), quoted in 78 Cong. Rec. 8584 (1934). On the floor of the Senate, Senator Steiwer objected to this proposed section on the ground that it would

"... create liabilities upon the issuing corporation in favor of investors who in one way or another may come in contact with the securities of the issuer. . . .
* * * I have heard no one deny that this amendment creates remote and unknown civil liabilities upon the issuing corporation."

The proposed section was thereafter deleted from the 1934 Act (*id.* at 8586), which indicates that Congress never intended to create liabilities against listed companies in favor of their security holders by reason of violation of stock exchange "rules" as plaintiffs urge here.

This deletion is analogous to that found significant by Judge Frankel in *DeRenzis v. Levy*, *supra*. There plaintiff

attempted to predicate liability on violation of a NYSE "rule" whose wording closely paralleled that of proposed but deleted sections of what became the Investment Advisers Act of 1940 (15 U.S.C. § 80b-1 *et seq.*). The Court found a "powerful and positive refutation of plaintiff's view" in the fact that the deleted sections, had they become law, would have served to achieve the result for which plaintiff contended and rejected the claim because it rested on "a kind of power of legislative revision which neither the SEC nor the courts nor a stock exchange may successfully assert against the paramount determination of the Congress." 297 F. Supp. at 1004. Obviously, this Court's obligation is " 'to make effective the congressional purpose' represented in 'the statute and the federal policy which it has adopted,' " *Colonial Realty Corp. v. Bache & Co.*, *supra* at 181, quoting from *J. I. Case Co. v. Borak*, 377 U.S. 426, 433 (1964). We submit that this Court should reaffirm its prior holding in *O'Neill v. Maytag* and refuse to open up an entirely new and unnecessary sphere of implied liabilities of issuers in favor of disappointed, but not defrauded, investors.

D. Assuming *Arguendo* That Boeing Did Not Comply With The Manual, Its Violation Was Non-Fraudulent And Not A Sufficient Basis For Implying A Cause Of Action Under The 1934 Act

Many cases have considered the problem of when a cause of action may properly be implied *against an exchange or NASD member* for violation of one of its "rules." These cases provide an independently sufficient reason to support the District Court's ruling that no cause of action may be implied for the kind of violation claimed here. Generally, as shown by a long and growing line of cases in this Circuit and elsewhere, the drastic step of implying a private cause

of action against an exchange or NASD member has been limited to those situations in which the plaintiff has been able to sustain a heavy burden by satisfying two criteria. First, he must demonstrate that the "rule" in question occupies such an integral position in the overall scheme of regulation and enforcement that (a) Congress meant to allow the SEC to impose liability, and (b) by refraining from exercising its own rulemaking authority, the SEC intended to substitute an exchange's "rule" for its own. Second, the acts claimed to be violative of the rule must be tantamount to the kind of fraud at which the 1934 Act is aimed. *See generally, Colonial Realty Corp. v. Bache & Co.*, 358 F.2d 178, 182 (2d Cir.), *cert. denied*, 385 U.S. 817 (1966). As the Court stated in *Hecht v. Harris, Upham & Co.*, 283 F. Supp. 417 (N.D. Cal. 1968), *modified on other grounds*, 430 F.2d 1202 (9th Cir. 1970), relying on the teaching of *Colonial Realty*:

"It has been held that, although there may be implied civil liability on the part of a broker under the Securities Exchange Act for violations of *certain kinds* of exchange or dealer association rules, (e.g., *rules which merely amount to a substitute for regulation by the S.E.C. itself*), *no implied civil liability may be predicated on rules which give power to discipline members for certain kinds of misconduct, including merely unethical behavior, which Congress could well not have intended to give rise to a legal claim, e.g., conduct which, although unethical under the association or exchange rules, does not amount to a fraud within the meaning of the fraud provisions of the Act itself.* *Colonial Realty v. Bache & Co.*, 358 F.2d 178 (2d Cir. 1966)." *Id.* at 431 (emphasis added).

In *Colonial Realty*, Judge Friendly, speaking for this Court, explained the fundamental and compelling policies behind the approach adopted. The first broad reason is that implying private causes of action will occasion an undesirable disruption of what has become an already complicated administrative and judicial regulatory scheme. *Id.* at 182; see also, *Landy v. FDIC*, 486 F.2d 139, 165-166 (3d Cir. 1973), *cert. denied*, U.S. , 40 L.Ed. 2d 312 (1974). The second is that any other treatment would "saddle the federal courts with garden-variety customer-broker suits" which ought to be decided in state courts. *Colonial Realty Corp. v. Bache & Co.*, *supra* at 183; see also, *Aetna Casualty & Surety Co. v. Paine, Webber, Jackson & Curtis*, CCH Fed. Sec. L. Rep. [1969-1970 Transfer Binder] ¶ 92,748 at p. 99,275 (N.D. Ill. 1970). Because of the strength of these policies, Judge Friendly warned in *Colonial Realty* that "the party urging the implication of a federal liability [must carry] a considerably heavier burden of persuasion [when an exchange rule is involved than] when the violation is of the statute or an SEC regulation." 358 F.2d at 182 (emphasis added). These have been the watchwords of all the cases decided after *Colonial Realty* and clearly plaintiffs have failed to meet their burden.

One of the most recent cases in point is *Rich v. New York Stock Exchange*, CCH Fed. Sec. L. Rep. ¶ 94,736 (S.D.N.Y. July 23, 1974), in which the Court refused to imply a cause of action against the NYSE for failure to enforce compliance by a member with one of its rules. While holding that plaintiffs could not prevail even on a non-fraudulent theory, Judge Brieant reached the unavoidable conclusion, as did the District Court here, that:

"[s]ince the Court in *Colonial* declined to adopt a *per se* rule with regard to the violation of Exchange

rules, our research has revealed no decision which has upheld a complaint based on such a claim unless the complaint also contained sufficient allegations of fraud. See *Starkman v. Seroussi*, CCH Fed. Sec. L. Rep. ¶ 94,600 (S.D.N.Y. June 19, 1974); *Schönholtz* [sic] v. *American Stock Exchange*, CCH Fed. Sec. L. Rep. ¶ 94,539 (S.D.N.Y. May 6, 1974)." *Id.* at p. 96,445.

The recent opinion by Judge Lasker in the *Schönholtz* case,¹⁵ noted by the Court in *Rich*, aptly summarizes the cases that have followed *Colonial Realty*:

"Judge Friendly's admonition [in *Colonial Realty Corp.*] has been taken seriously by other courts presented with the same issue: no case of which we are aware has found an implied right of action for the violation *per se* of an exchange rule; allegations of such violation have been held to state a claim only where coupled with sufficient allegations of fraud on the investor. *Buttrey v. Merrill Lynch, Pierce, Fenner & Smith*, 410 F.2d 135 (7th Cir. 1969), cert. denied 396 U.S. 838, 90 S.Ct. 98, 24 L. Ed.2d 88 (1969) (N.Y.S.E. Rule 405, the 'know your customer rule,' actionable in conjunction with allegations of fraud), *Aetna Casualty & Surety Co. v. Paine, Webber, Jackson & Curtis*, '69-'70 Transfer Binder, CCH Fed. Sec. L. Rep. ¶ 92,748 (N.D. Ill. 1970) (alleged violation of Rule 405 amounting to mere negligence failed to state a claim) *accord*, *McMaster Hutchinson & Co. v. Rothschild & Co.*, 1972-73 Transfer Binder, CCH Fed. Sec. L. Rep.

¹⁵ 376 F. Supp. 1089 (S.D.N.Y. 1974).

¶ 93,541 (N.D. Ill. 1972) ; *Bush v. Bruns Nordeman & Co.*, 1972-73 Transfer Binder, CCH Fed. Sec. L. Rep. ¶ 93,674 (S.D.N.Y. 1972) (alleged violations of Rule 405 'inextricably linked' with § 10b claims stated a claim). These cases guide us here. Since we have found that plaintiff has failed to state a § 10b claim, his allegations regarding violation of Amex rules, taken alone, do not state a claim." *Id.* at 1092.

Plaintiffs have attempted to avoid this overwhelming contrary authority by improperly relying on the Seventh Circuit's decision in *Buttrey v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 410 F.2d 135 (7th Cir.) *cert. denied*, 396 U.S. 838 (1969) (Kass Goodkind Brief at 34-36; 50-53).¹⁶ In that case, one Dobich, President of Dobich Securities Corporation, had set up a cash account with defendant (a NYSE member firm) through which he bought and sold securities. Plaintiff, the trustee in bankruptcy for Dobich Securities, alleged that Merrill Lynch knew that Dobich had used property fraudulently converted from his company's customers and yet allowed the transactions to continue. In separate counts the acts of Merrill Lynch were claimed to be (1) an aiding and abetting of Dobich's fraud; (2) an independent violation of Section 17 of the 1933 Act and Rule 10b-5; and (3) a breach of its duty under NYSE

¹⁶ Plaintiffs make no serious contention that Boeing's claimed violation was fraudulent. Instead, they attempt to equate the facts here with the facts in *Buttrey* rightly classified by the Seventh Circuit as "tantamount to fraud." It is difficult to take this contention seriously inasmuch as the facts in *Buttrey* (trading in securities known to have been fraudulently converted by one's customer) are light years removed from the facts claimed (and rejected by the fact finder) here ("knowledge" of Section A 10 of the Manual and noncompliance). See Kass Goodkind Brief at 34-50.

Rule 405 (the "Know Your Customer Rule"). The Seventh Circuit held that all three counts pleaded causes of action and stated with respect to the alleged Rule 405 violation:

"Although mere errors of judgment by defendant might not support a federal cause of action, the facts alleged here are *tantamount to fraud* on the bankrupt's customers, thus giving rise to a private civil damage action. See *Hecht v. Harris Upham & Co.*, 283 F. Supp. 417, 430, 431 (N.D. Cal. 1968)." *Id.* at 143 (emphasis added).

The Court below quite correctly pointed out the vast difference between the violation in *Buttrey* and the claimed violation here for which plaintiffs urge liability (312a-313a). *Buttrey* is a case in which plaintiff made it past the pleading stage because he charged that defendant knowingly perpetrated a fraud. Obviously, only where the violation claimed brings the case within the ambit of the 1934 Act may a cause of action be implied, and just as obviously the scope of the 1934 Act is limited. As the Court said in *Mercury Investment Co. v. A.G. Edwards & Sons*, 295 F. Supp. 1160, 1163 (S.D. Tex. 1969), quoting from *Hecht v. Harris, Upham & Co.*, *supra* (283 F. Supp. at 430):

"[T]he Security [sic] Acts . . . are essentially directed at *fraud*—not against mere negligence or errors of judgment on the part of the broker. * * * Nor do mere irregularities or carelessness render [a broker] liable for fraudulent breach of trust." (Emphasis in original).

The District Court's reading of *Buttrey* accords with that of all other cases of which we are aware, which have also

limited its scope to fraud. In addition to the recent opinions of Judges Brieant and Lasker, *supra*, see also, *Wells v. Blythe & Co., Inc.*, 351 F. Supp. 999, 1001 (N.D. Cal. 1972); *McCurnin v. Kohlmeyer & Co.*, 347 F. Supp. 573, 576 (E.D. La. 1972), *aff'd* 477 F.2d 113 (5th Cir. 1973); *McMaster Hutchinson & Co. v. Rothschild & Co.*, CCH Fed. Sec. L. Rep. [1972-1973 Transfer Binder] ¶ 93,541 (N.D. Ill. 1972). To the same effect, see *McCormick v. Esposito*, CCH Fed. Sec. L. Rep. ¶ 94,795 at pp. 96,643-44 (5th Cir. September 13, 1974).

Plaintiffs assert that these cases have misinterpreted *Buttrey*. They cite cases which purportedly establish that fraud need not be alleged before a cause of action may be implied but none of them supports their position (Kass Goodkind Brief at 37-42). For instance, in *SEC v. First Securities Co. of Chicago*, 463 F.2d 981 (7th Cir.), *cert. denied, sub. nom., McKy v. Hochfelder*, 409 U.S. 880 (1972) (cited in Kass Goodkind Brief at 37), the claims against defendant (an NASD member) arose because its president and 92% owner, Lester Nay, defrauded his and his firm's clients by inducing them to place their money in a "spurious" escrow investment account. Nay killed himself, leaving a suicide note describing his thefts. It was claimed that Nay's firm was responsible for his thefts on three theories: that it was "a controlling person" of Nay, that it aided and abetted his fraud, and that its failure to supervise Nay (in violation of NASD rules) allowed his fraud to continue. The Seventh Circuit held that all three theories supported liability. It is somewhat disingenuous of plaintiffs to suggest, as they do, that *First Securities* is a case in which no fraud was present (Kass Goodkind Brief at 37). In fact, the Court, having held that *First Securities* was liable as an aider and abetter had little difficulty in reaching its holding to which plaintiffs attach such importance;

namely, that "First Securities is properly liable for Nay's fraud because of its violation of Rule 27 of the N.A.S.D." 463 F.2d at 988 (emphasis added).

Plaintiffs' reliance on Judge Weinfeld's recent decision in *Starkman v. Seroussi*, 377 F. Supp. 518 (S.D.N.Y. 1974), is similarly misplaced (Kass Goodkind Brief at 37-38). *Starkman* was a suit by a customer against a NYSE member firm, one of its registered representatives and the latter's daughter, alleging implied causes of action under the 1934 Act based on violations of NYSE Rule 345.17 (prohibits a registered representative from guaranteeing a customer against loss in his account), NYSE Rule 345.19 (requires members to make thorough background checks of those they contemplate employing) and NYSE Rule 405 (the "Know Your Customer Rule"). The Court granted plaintiff's motion to stay arbitration, holding nothing more than that:

"Plaintiff's allegations, which specify the details of violations of the Stock Exchange rules by the defendants, are by no means 'immaterial' or 'insubstantial' and upon their face are sufficient to confer jurisdiction under section 27 of the Exchange Act. Plaintiff consequently has 'the right to select the judicial forum' in which to prosecute his suit and, in view of section 29 of the Exchange Act, cannot be compelled to submit his claim to arbitration." *Id.* at 524 (footnotes omitted).

Plaintiffs simply are in error when they state in their brief that "Judge Weinfeld found liability. . . ." (Kass Goodkind Brief at 38). What the Court did say was that plaintiff might make the argument that defendants' acts:

". . . were part of a scheme or device to evade the Stock Exchange rules and thereby defraud plaintiff.

. . . The alleged violations of the Exchange rules are such an integral part of the transaction as to constitute a sufficient claim for violation of sections 6 and 19 of the Exchange Act." *Id.* at 524 (emphasis added; footnote omitted).

What Judge Weinfeld did in *Starkman* was simply follow the teaching of *Colonial Realty* to jump the initial jurisdictional hurdle and suggest to plaintiff an argument whereby he could try to prove defendants' *fraud*.

Plaintiffs also cite the clearly inapposite case of *Isaacs v. Chartered New England Corp.*, CCH Fed. Sec. L. Rep. ¶ 94,708 (S.D.N.Y. June 28, 1974), in an effort to overturn the holding of the Court below that mere negligence will not support an implied federal claim (Kass Goodkind Brief at 38). In *Isaacs* the Court was not presented with the issue of implication of a cause of action based on violation of an exchange or NASD rule and did not even attempt to draw an analogy to cases implying such causes of action. There, Tessler (an employee of Chartered, a NYSE member firm) and one Feeney engaged in a scheme to manipulate the market in Coatings stock, for which Chartered acted as a market-maker. Both men had pleaded guilty to criminal conspiracy charges. It was claimed that Chartered and Tessler "fraudulently induced plaintiff to purchase shares of stock of [Coatings], through the use of manipulative and deceptive devices and contrivances' in violation of the 1933 Act, the 1934 Act, the Rules of the Securities and Exchange Commission ('SEC') and common law." *Id.* at p. 96,335 (emphasis added). Judge Bonsal held Chartered liable for the *fraud* committed, either as a controlling person of Tessler or under a *respondeat superior* theory. *Id.* at p. 96,337 n.1. Obviously, the case has no bearing whatever on the issue at Bar.

Plaintiffs also attempt to distinguish *Bush v Bruns Nordeman & Co.*, CCH Fed. Sec. L. Rep. [1972-1973 Transfer Binder] ¶ 93,674 (S.D.N.Y. 1972), a case properly relied on by the Court below to support its holding that negligent violations of exchange rules are not actionable (Kass Goodkind Brief at 39). *Bush* involved defalcations by an employee of a bankrupt NASD member firm, represented in the action by its trustee in bankruptcy. It was alleged that defendant's acts, including violations of the NYSE's "Know Your Customer Rule," allowed conversion and fraud to be perpetrated. The Court stated that "[t]he alleged anti-fraud violations of federal securities law are inextricably linked with [the purported violation of Rule 405]." *Id.* at pp. 93,007-08. All that Judge Palmieri held was that the alleged violation, since it was "inextricably linked" to the fraud, could not be dismissed *per se* at the pleading stage. Thus, the *Bush* case is clearly in line with the mandate of *Colonial Realty* and all other subsequent cases, which have read that decision in the same manner as the Court below and as urged here by Boeing.

E. The District Court Correctly Held That Plaintiffs Cannot Recover On A Third Party Beneficiary Theory

As discussed above, the District Court determined that Boeing did not breach its Listing Agreement with the NYSE. Since there was no breach, there can be no recovery either by the Exchange, as a party to that contract, or by plaintiffs, even if they were third party beneficiaries of the Listing Agreement.

Nor is plaintiffs' claim enhanced by the Manual. First, the Court found that Boeing complied with the Manual provisions so that there was no breach of contract (312a). Even assuming *arguendo* that there was a breach, it was

not material. See *Jacob & Youngs, Inc. v. Kent*, 230 N.Y. 239, 129 N.E. 889 (1921). Moreover, the Manual is not part of Boeing's contract with the Exchange and plaintiffs cannot recover on a contract theory without first proving the existence of a contract.

Even if Boeing had breached its Listing Agreement (or the Manual if that had been part of its contract with the Exchange), plaintiffs still cannot recover as third party beneficiaries. The remedies afforded to a third party beneficiary as such can be no greater than, or different from, the remedies available to the promisee:

"The remedies available to a beneficiary are exactly the same as would be available to him if he were a contractual promisee of the performance in question." 4 A. Corbin, *Contracts* § 810 at 230 (1951).

See also, 2 S. Williston, *Contracts* § 364A (3d ed. Jaeger, 1959). The sole remedy for a breach, if there were one, would be with the Exchange and that is delisting. See *supra* at 41-42. To create a remedy in damages for these plaintiffs, where no such remedy is available to the NYSE as promisee, would be to rewrite the contract to the substantial detriment of Boeing as promisor.

This case is clearly distinguishable from *Weinberger v. New York Stock Exchange*, 335 F. Supp. 139 (S.D.N.Y. 1971), where the Court held that the plaintiff investor stated a cause of action against the NYSE as a third party beneficiary of the NYSE's agreement made pursuant to § 6(a) (1) of the 1934 Act requiring the NYSE to seek compliance by its members with the provisions of the 1934 Act and its rules. The Court reasoned that the imposition of liability upon the NYSE based upon a claim asserted by an investor was proper

"[s]ince [as] the Exchange is already liable for any breach of its statutory duty, the imposition of a virtually coterminous contractual duty will not have the disruptive effect of an unexpected civil liability, which is sometimes seen as an argument against third-party recovery, *e.g.*, *Moch Co. v. Renssalaer Water Co.*, 247 N.Y. 160, 159 N.E. 896 (1928)." *Id.* at 144 n. 10.

Here, imposition of third party contractual liability upon Boeing would not be coterminous with any statutory duty owed by Boeing—there is no such statute or duty. Moreover, it would have exactly "the disruptive effect of an unexpected civil liability" that concerned Judge Gurfein in *Weinberger*.

Furthermore, plaintiffs cannot recover as third party beneficiaries since they are the direct promisees of another contract, namely the Indenture and debenture, which set out detailed notice procedures different from those of both the Listing Agreement and the Manual. Since Boeing clearly complied with its contractual obligations to plaintiffs under the Indenture and debenture, which the Court held are "the only contracts between plaintiff debenture holders and BOEING" (312a), plaintiffs cannot raise an inconsistent gratuitous obligation assumed by Boeing (assuming *arguendo* that the Manual is an obligation) as the basis for an independent claim.

"No case has gone so far as to hold that, where the person for whose benefit the contract is made, has himself or by his privy in estate entered into a contract inconsistent with this, he may repudiate such prior contract, and claim the benefit of the second simply because it has become for his interest to do so. We know of no principle which authorizes one

party to an agreement to vary it, even against his own interest, without the consent of the other." *Constable v. National Steamship Co.*, 154 U.S. 51, 73 (1894).

See also, 17 Am. Jur. 2d, Contracts § 302.

Finally, plaintiffs' third party beneficiary claim must fail because there was no causative link between Boeing's alleged breach and plaintiffs' claimed damages.

In *Rochester Lantern Co. v. Stiles & Parker Press Co.*, 135 N.Y. 209, 217, 31 N.E. 1018, 1021 (1892), the Court of Appeals said:

" . . . damages must flow directly and naturally from the breach of the contract, and they must be certain, both in their nature and in respect of the cause from which they proceeded. Under this . . . rule, speculative, contingent and remote damages which cannot be directly traced to the breach complained of are excluded."

Similarly, in *Hart v. United Artists Corp.*, 252 App. Div. 133, 139, 298 N.Y.S. 1, 7 (1st Dep't 1937), the Court said ". . . damages must be certain not only in their nature and quantity but clear in respect of the cause from which they proceed" and noted that there must be "some proof that such loss flowed from the breach." More recently in *Transamerican Mercantile Corp. v. Western Union Telegraph Co.*, 156 N.Y.S.2d 201, 205-06 (N.Y. City Ct. 1955), modified on other grounds, 153 N.Y.S.2d 771 (App. Term 1st Dep't 1956), the Court noted that

"[i]t is the established rule of the law of damages that a defendant is liable only for such damages as are the natural and direct or proximate conse-

quences of his wrongful acts or omissions. The rule is applicable to cases of contract as well as tort. . . ."

Thus, even if Boeing had a duty to issue a general news release in the first week of March, 1966, and breached it, and assuming the Court's factual finding of substantial compliance is "clearly erroneous," plaintiffs offered no proof whatsoever that Boeing's failure to issue such a release caused their loss. Without at least some proof that Boeing's acts caused loss to plaintiffs, they cannot prevail here. *See generally*, Malone, "Ruminations on Cause-In-Fact," 9 Stan. L. Rev. 60 (1956); Restatement (Second) of Torts § 433B (1965).

IV

**THE DISTRICT COURT'S CONDUCT OF THIS
NON-JURY TRIAL, LARGELY ON AN AGREED
STATEMENT OF FACT, IN NO WAY DEPRIVED
PLAINTIFFS OF THE ESSENTIAL FAIRNESS TO
WHICH THEY ARE ENTITLED**

Finally, plaintiffs complain that the District Court's alleged hostility to their counsel, combined with the procedures it established for the examination of witnesses (the lawyer who began examination of a witness was required to conduct the entire examination of that witness), require reversal of the judgment entered below and the granting of a new trial (Kass Goodkind Brief at 61-67). In support of this claim of misconduct, plaintiffs quote out of context certain colloquy between the Court and counsel claimed to be an "abusive tirade" showing "shocking hostility." (*Id.* at 61-62).

Obviously, a district court judge must have wide discretion with regard to the conduct of trial proceedings in order to insure that they proceed with evenness and expedition. In this light, the Court's ruling that each witness be examined by a single lawyer for each side—a ruling made in the opening minutes of the trial so that plaintiffs' counsel had ample opportunity to adjust their strategy (316a-318a)—was an appropriate exercise of discretion.¹⁷ Rather than

¹⁷ The complaint in this consolidated action was filed June 23, 1966, and was signed by all three attorneys who represented plaintiffs at the four day trial, which began on November 15, 1972 (33a). Surely in this more than six year interval plaintiffs' attorneys became (or should have become) well-versed in all phases of the case. It is worth noting that on April 4, 1969, both Mr. Winer and Mr. Wechsler attended (685a-686a) and propounded questions (688a; 783a) at the deposition of Harold W. Haynes and both attorneys attended and propounded questions at the deposition of Harold F. Olsen (813a; 824a)—two of the principal witnesses who testified at trial and the only ones whom plaintiffs deposed.

accepting the Court's decision, plaintiffs' counsel repeatedly raised the issue (*e.g.* 464a-471a; 556a) and, quite understandably, this practice provoked the Court's criticism, which plaintiffs now claim constitutes judicial impropriety. As two of the leading commentators have said in stating the rule applicable to such charges: "Motions raising this ground happily are rare and a new trial is not required if the judge's behavior has not made the trial unfair." 11 C. Wright & A. Miller, *Federal Practice & Procedure: Civil* § 2809 at p. 66 (1973). See *DiBello v. Rederi A/B Svenska Lloyd*, 371 F.2d 559, 561 (2d Cir. 1967) (trial judge's comments in jury case "insufficient to contaminate the free air of an impartial tribunal or to necessitate reversal"). A claim of judicial misconduct was raised in *Cohen v. Franchard Corp.*, 478 F.2d 115 (2d Cir.), *cert. denied*, 414 U.S. 857 (1973), and, while each case involves its own peculiar facts, the language of this Court in that case is particularly apt here:

"... the conduct complained of was far from unprovoked. The alleged improper acts strike us as appropriate responses by a conscientious judge in handling difficult situations created largely by the lack of preparation for trial and evasive attitude toward the judge by appellants' counsel." *Id.* at 125.

We submit that plaintiffs' claim for a new trial is totally without merit and should be rejected in its entirety.

CONCLUSION

The judgment of the District Court should be affirmed in all respects.

Dated: New York, New York
October 9, 1974

Respectfully submitted,

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APPENDIX

PAGINATION AS IN ORIGINAL COPY

Opinion of Ryan, D.J. Dated November 29, 1973

UNITED STATES DISTRICT COURT

SOUTHERN DISTRICT OF NEW YORK

OPINION

66 Civ. 1820

WILLIAM R. VAN GEMERT, et al.,

Plaintiffs,

—v.—

**THE BOEING COMPANY (formerly
BOEING AIRPLANE COMPANY), et al.,**

Defendants.

**NATHAN, MANNHEIMER, ASCHE, WINER & FRIEDMAN,
ESQS., and IRVING STENMAN, ESQ., New York, New
York, Attorneys for Committee of Plaintiffs (NORMAN
WINER, IRVING STEINMAN, and SAMUEL WILKSTEIN,
Esqs., of Counsel).**

**KASS, GOODKIND, WECHSLER & GERSTEIN, ESQS., New
York, New York, Attorneys for Plaintiffs (STUART D.
WECHSLER and MICHAEL P. FUCHS, Esqs., for Counsel).**

**DAVIS, POLK & WARDWELL, ESQS., New York, New York,
Attorneys for Defendants (S. HAZARD GILLESPIE and
WILLIAM H. LEVIT, JR., Esqs., of Counsel).**

Opinion of Ryan, D.J. Dated November 29, 1973

RYAN, J.:

This is a consolidated class action brought by former and present holders of unregistered convertible debentures issued by BOEING COMPANY to recover for losses arising out of the Company's refusal to convert the debentures after March 29, 1966, the expiration date set by it for the exercise of conversion rights.

Originally, separate actions were filed by various plaintiffs against defendant and its directors in California, Pennsylvania, Florida and Washington, D.C. By order of October 4, 1966, these ten actions were ordered maintained as class actions; a consolidated amended complaint was filed and a consolidated trial had. The order declared the action brought "on behalf of a class comprised of plaintiffs and all other present and former holders of The Boeing Company (formerly Boeing Airplane Company) 4-1/2% convertible subordinated debentures due July 1, 1980 and calls for redemption on April 8, 1966, whose debentures were not surrendered for conversion on or before March 29, 1966." The class represents but 7.2% of all the holders, aggregating \$1,544,300. out of a total of \$20,085,700. who did convert.

Trial was had before the Court on an agreed statement of facts, which was subject only to objections as to relevancy and materiality and to further testimony by witnesses.

The complaint contains thirteen counts and charges violations of the Securities Act of 1933, the Securities Exchange Act of 1934, the

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Trust Indenture Act of 1933 and common law breach of contract.

The principal claims raised by the complaint are:

1. That BOEING forfeited its right to terminate plaintiffs' option to convert the debentures because it breached its contract with plaintiffs in that it failed (a) to change and publish the conversion rate as required by the Indenture; (b) to file with the Trustee under the Indenture a statement setting forth the new rate; and (c) to set aside sufficient shares to satisfy the conversion at the new rate. These requirements, plaintiffs allege, were conditions precedent to exercising the call. Plaintiffs contend that the conversion rate of 2 shares for one debenture should have been adjusted to 2.07 shares for one debenture.

2. That the nature of the call given by defendants was insufficient for the ordinary person, in view of the fact that the Indenture was a contract of "adhesion", and that this is the test to be applied, and not whether the notice satisfied the language of the Indenture.

3. That the defendants failed to comply with the Rules of the New York Stock Exchange respecting publicity on calls, which rules were tantamount to a contract for the benefit of plaintiffs as investors and third party beneficiaries.

The damages sought are \$4,380,937.82 with interest at 7%, which, it is alleged, represent the value of the debentures held by plaintiffs as well as benefits accrued and lost by way of rights to purchase more stock and debentures, a two-for-one stock split and dividends.

Plaintiffs have attempted to enlarge the class by seeking damages for those bondholders who did convert on time, on the theory that they suffered losses by the alleged failure of defendants to adjust the conversion rate. The court refuses to consider this claim as the order clearly defines the class, and, in fact, plaintiffs' complaint states that suit is brought on behalf of "all holders of debentures who did not convert on or before

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March 29, 1966."

Plaintiffs would also include in the class those who redeemed after March 29, 1966, on the theory that, under the adjusted rate of conversion, they were entitled to more shares than they received. It is unnecessary to pass upon the merits of this claim in view of our final determination that the class cannot prevail.

I find the following facts to be established by the evidence.

On June 23, 1958, THE BOEING COMPANY authorized the issuance and sale of its 4-1/2% Convertible Subordinated Debentures, due July 1, 1980, in the aggregate principal amount of \$30,597,600. The debentures were issued pursuant to a subscription offer to shareholders of record at the close of business on July 15, 1958. By the subscription offer, each shareholder was given the right to subscribe to the debenture offer in the ratio of \$100. principal amount of debenture for each 23 shares of capital stock held on the record date. City Bank-Farmers Trust Company, the subscription agent, mailed 7,037,448 warrants and prospectuses to all stockholders of record. This list of stockholders was kept by the Agent for six years for the purpose of paying dividends and then destroyed in 1964. The warrants, which were exercised by tender to the Agent, were retained until 1966 and are now in the possession of the successor Agent. Each warrant bears the name and address of the stockholder, the number of rights exercised and, if transferred, the name and address of the transferee. BOEING never had a copy of the stockholder list or of the cancelled checks.

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During the period of the offer, a total of \$29,578,000. in full payment of debenture subscriptions was received by City Bank. The total amount of unsubscribed debentures purchased by the underwriters was \$1,019,000.

By resolution dated July 14, 1958, the Board of Directors of BOEING set the initial conversion rate for the debentures at two shares of capital stock for each \$100 principal amount of debentures, equivalent to a conversion price of \$50 per share of capital stock. BOEING reserved 611,952 shares for issuance and in consideration of the surrender for conversion of debentures at this initial conversion rate. The debentures were issued under an Indenture dated July 1, 1958 between BOEING and The Chase Manhattan Bank, Trustee, and under a registration statement filed with the Securities Exchange Commission. The debentures were listed in the New York Stock Exchange under a Listing Agreement, which included a copy of the Indenture.

The debentures were unsecured obligations of BOEING maturing on July 1, 1980 and bearing interest from July 29, 1958 at 4- $\frac{1}{2}$ % payable semi-annually on January 1 and July 1. They were issued in both coupon and fully registered form, and provision was made that the coupon debentures, at the option of the holder, could be registered as to principal only. This privilege to register was stated twice on the face of the debenture, as well as in several places in the Indenture. Unregistered coupon debentures were transferable by delivery; fully registered debentures and registered coupon debentures were transferable by presentation to the Trustee with appropriate endorsement or written instrument of transfer.

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The coupons of the coupon debentures, which had been registered as to principal, continued to be payable to bearer and transferable by delivery.

The debentures stated (second paragraph) that they were issued under the Indenture of July 1, 1958 "to which Indenture . . . reference is hereby made for a description of the rights, limitations of rights, obligations, duties and immunities thereunder of the Trustee, the Company and the holders of the Debentures and coupons."

The debentures also called attention to the expiration of the conversion rights ten days prior to the redemption date and specifically incorporated by reference the Indenture provisions relating to the notice of redemption, which read:

"The holder of this Debenture is entitled, at his option, at any time on or before July 1, 1980, or in case this Debenture shall be called for redemption prior to such date, then to and including but not after the tenth day prior to the redemption date, to convert this Debenture . . . at the principal amount hereof . . . into shares of Capital Stock of the Company, at the conversion rate of two shares of Capital Stock for each \$100 principal amount of Debentures. . . . The Debentures are subject to redemption . . . at any time or times, at the option of the Company, on not less than 30 nor more than 90 days' prior notice, as provided in the Indenture . . .".

This was followed by a table entitled "If Redeemed During the 12 Months' Period Ending July 1" (large black letters) setting forth clearly the redemption prices at various dates including the instant date.

The Indenture is a 113 printed page book, which sets forth in extenso the rights and duties of the Company, the Trustee and the Debenture holders, and defines all the terms used.

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Thus, Article One, Sec. 1.01, defines Conversion Rate as:

"the number of shares of Capital Stock into which each \$100 principal amount of Debentures may be converted as hereinafter in Article Four provided."

Article Four, Sec. 4.04, states that the Conversion Rate at which Capital Stock shall be issuable upon conversion of debentures shall be "2 shares of Capital Stock for each \$100 principal amount of debentures, the conversion rate being subject to adjustment."

Section 4.05 provides a formula for adjusting the conversion rate in the event certain types of action might be taken by BOEING, including, among others not relevant here, declaration of stock dividends, limited stock dividends and acquisitions and issuance of shares for a consideration other than cash. It provides that, in computing the adjustment if the Company shall issue any capital stock after July 1, 1958, there should be excluded "up to 350,000 shares" (after having been adjusted on the basis of stock dividends) "which may be issued after July 1, 1958 pursuant to the Company's Stock Option Plan or Incentive Compensation Plan for Officers and Employees", and the conversion rate shall be adjusted as follows:

"\$100 shall be multiplied by the number of Capital Stock outstanding after any such issuance . . . and the resulting product shall be divided by the aggregate consideration, determined in accordance with subparagraph (b) of this Section 4.05, received by the Company for its shares of Capital Stock then outstanding The resulting quotient adjusted to the nearest one-hundredth, shall thereafter be the conversion rate if it is greater than the basic conversion rate. If the resulting quotient . . . is less than the basic conversion rate . . . the conversion rate shall be the basic conversion rate."

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Section 4.05(b) also provides that the aggregate consideration referred to above shall be \$351,872,350 plus any additional consideration received after July 1, 1958 determined as follows:

“(iv) In the case of shares issued as a Limited Stock Dividend the consideration shall be deemed to be the number of shares so issued multiplied by the market value thereof (as defined in Sec. 1.01) on the date of the declaration thereof.”

Section 1.01 defines market value of a Limited Stock Dividend as the last reported sale price of the Capital Stock on the New York Stock Exchange on the date of the declaration of each stock dividend.

Section 4.05(b)(ii) further provides that, in the case of the issuance of shares for a consideration in whole or in part other than cash, the consideration other than cash shall be deemed to be the fair value thereof as determined by the Board of Directors.

Section 4.05(f), in addition, provides that, whenever the amount by which the conversion rate would be changed is less than one-twentieth of a share of capital stock, the Company need not make such adjustment; but, whenever that amount would be changed to more than one-twentieth of a share of capital stock, the Company shall be required to make at that time only that part of such adjustment which will result in changing the conversion rate by the largest possible multiple of one-twentieth of a share of capital stock. Simply put, this means that, if shares of stock are issued for less than \$50 a share, an adjustment in the conversion rate may be required and that the formula provides for multiplying the number of shares outstanding by \$100 and dividing such figure by the total consideration received

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for all shares; if the quotient obtained is more than 2.05, an adjustment in the conversion rate is required.

The Indenture further provided that:

"Whenever the Company shall make any adjustment in the conversion rate as herein provided, the Company shall forthwith (a) file with the Trustee and any conversion agent a statement, signed by the president or any vice president of the Company and by its treasurer or an assistant treasurer, showing in detail the facts requiring such adjustment and the conversion rate that will be effective after such adjustment and (b) publish at least once in an Authorized Newspaper a notice stating that the conversion price has been adjusted and setting forth the adjusted conversion price."

Article Five is of special importance for it deals with redemption of the debentures and sets forth the requirements, for notice, as follows:

"Section 5.02. Notice of Redemption; Partial Redemptions. In case the Company shall desire to exercise the right to redeem all or any part of the Debentures, as the case may be, pursuant to Section 5.01, it shall publish prior to the date fixed for redemption a notice of such redemption at least twice in an Authorized Newspaper, the first such publication to be not less than 30 days and not more than 90 days before the date fixed for redemption. Such publication shall be in successive weeks but on any day of the week. It shall not be necessary for more than one such publication to be made in the same newspaper. A copy of such notice shall be mailed by the Company at least 30 days prior to such redemption date to the holders of the registered Debentures without coupons and the holders of the coupon Debentures registered as to the principal so to be redeemed at their last addresses as they shall appear upon the registry books, but failure to give or receive such notice by mail, or any defect therein, shall not affect the validity of any proceedings for the redemption of Debentures.

"An 'Authorized Newspaper' is defined in Section 1.01 of the Indenture as follows:

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"Authorized Newspaper

The term 'Authorized Newspaper' shall mean a newspaper printed in the English language and customarily published at least once a day for at least five days in each calendar week and of general circulation in the Borough of Manhattan, The City of New York, New York, whether or not such newspaper is published on Saturdays, Sundays and legal holidays."

Pursuant to section 7.03 of the Indenture, the Chase Manhattan Bank, as interest paying agent for the debentures, received generally semi-annually and otherwise from time to time coupons which had been detached from the debentures and tendered for the collection of interest. A vast majority of the coupons tendered to the Chase Manhattan Bank came from collecting banks, and Chase Manhattan did not know the identity of the holders of the debentures on whose behalf the coupon tenders were made.

Sections 8.01 and 8.02 of the Indenture require that BOEING give to Chase Manhattan the names and addresses of additional debenture holders who become known to BOEING and its paying agent other than the Trustee. From 1959 to 1966, no such information came to the knowledge of BOEING and it gave none to the Trustee.

I find that, during January and February, 1966, BOEING's Directors and Investment Banking Advisors discussed the possibility of broadening BOEING's stock base in order to meet its requirements for additional capital needed for plans of building up its jet and supersonic jet transport programs. Of several alternatives discussed, it was determined that calling the debentures for redemption was the best way of raising additional capital while affording the debenture holders an opportunity to participate in a

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rights offering, and thus broaden BOEING's stock base. On February 24, 1960 at a meeting with Haynes, BOEING's vice president for finance, Thornton, its treasurer, and its Counsel, a possible time schedule for giving notice was discussed, with first publication of the notice of redemption on March 7 or 8, 1966, expiration of the right of conversion on March 29, 1966, and redemption on April 6, 1966. At this meeting, it was decided that Olsen, a member of the firm of counsel for BOEING, should prepare drafts of resolutions for the Board meeting scheduled for February 28, 1966 to authorize an increase in the authorized capital stock, the making of a rights offering of capital stock or securities convertible into capital stock, the issuance of a two-for-one stock split and a call of the debentures for redemption on February 24, or 25, 1966.

Olsen, BOEING's investment bankers and the latter's counsel, discussed as a tentative time schedule that the first publication of the notice of redemption would be on March 7, 1966; that the conversion privilege would expire on March 28, 1966; and that the redemption of the debentures would be on April 6, 1966. On February 27, 1966, Allen, Haynes and Olsen reviewed the draft resolutions which Olsen had prepared for the February 28, 1966 meeting of the Board and the tentative time schedule and a draft press release with respect to several items, including the call for debentures.

On February 28, 1966, Thornton called a Corporate Trust Officer at Chase Manhattan Bank and told him that the Board probably would authorize a call of the debentures for redemption at its meeting that day and advised

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him to be prepared for redemption of the debentures. A "Tentative Timetable" dated February 28, 1966, prepared by counsel Olsen, was distributed to and reviewed by the Directors who adopted the following resolution:

"Resolved, that the President, Vice President—Finance, or Treasurer of the Company, or any one of such officers, is hereby authorized to take all such action as they or any one of them deems appropriate or necessary to call for redemption on a date to be selected by them or any one of them, all of the 4½% Convertible Subordinated Debentures of the Company then outstanding under the Indenture dated July 1, 1958, between Boeing Airplane Company and The Chase Manhattan Bank, Trustee."

On February 28, 1966, the Boeing News Bureau issued News Release S-8726 headlined "Boeing Reports 1965 Sales, Net Earnings" and marked "For Immediate Use" which, in part, stated that, at the Board of Directors' meeting held that day, "the Company's management was also authorized to call for redemption at a future date all of the Company's outstanding 4½% convertible subordinated debentures." The release was issued as early as possible, after Board action, to the financial editors of the New York Times, the New York Herald-Tribune, the Wall Street Journal and other major national newspapers, to the Associated Press and the United Press International, to Dow Jones and Company, Inc., to Seattle area newspapers, to aerospace publications and others. On March 1, 1966, BOEING sent a teletype to the New York Stock Exchange, advising it that the Board had authorized its officers to call the debentures for redemption, but that the redemption date had not been established, and it confirmed this advice in a letter to the Exchange dated March 2, 1966. On March 1, 1966, Raftery of the Exchange was

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advised by Olsen that no dates had yet been set for the call; that the resolution of the Board on February 28 had fixed no date but merely authorized BOEING to set the dates; that meetings were scheduled to commence on March 2, 1966 with BOEING's investment bankers and their counsel to develop plans for upcoming financing; and that he would be advised of the dates for the call as soon as they were fixed. However, prior to the meeting of February 28, 1966, Olsen had called Shriver of the Exchange and reviewed with him on a preliminary and confidential basis the tentative time table for the call and obtained his approval.

On March 3, 1966, Chase Manhattan sent BOEING for review and approval a draft of the contemplated notice which had been prepared by counsel for Chase Manhattan in accordance with its practice. Between March 2, and 7, 1966, the tentative dates discussed for the call were: first publication on March 8; expiration of conversion March 29; and redemption April 8, 1966. By March 7, 1966, the firm dates were fixed as March 8 and 18 to be published in all editions of the Wall Street Journal. Olsen then called Raftery of the Exchange, informed him of the dates, and requested him to put them on the Dow Jones Tape and the ticker, which Raftery agreed to do. This Olsen, of counsel for BOEING, considered compliance with the publicity requirements of the Exchange (Section A-10 of the New York Stock Exchange Manual).

I find that on March 8 and 18, 1966, notice of redemption of the debentures, including a statement that the "right of conversion will terminate at the close of business on March 29, 1966", was published by BOEING

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in all editions of the Wall Street Journal, viz., the Eastern, Mid-Western, Pacific Coast and Southwestern editions, in the form set forth herewith:

The Boeing Company

(formerly Boeing Airplane Company)

Notice of Redemption of

4½ % Convertible Subordinated Debentures, due July 1, 1980

NOTICE IS HEREBY GIVEN that, pursuant to the provisions of the Indenture dated July 1, 1958, between Boeing Airplane Company (now The Boeing Company) (hereinafter called the Company) and The Chase Manhattan Bank (now The Chase Manhattan Bank [National Association]), Trustee, the Company has exercised its option to and will redeem, on April 8, 1966, all of its outstanding 4½ % Convertible Subordinated Debentures, due July 1, 1980 (hereinafter called the Debentures), at the redemption price of 103.25% of the principal amount thereof, together with accrued interest to said redemption date.

On and after April 8, 1966, interest on the Debentures shall cease to accrue and the coupons for interest maturing after said date shall be void.

Payment of the redemption price, with accrued interest to the date fixed for redemption, will be made at the principal office of the Trustee upon presentation and surrender for redemption, on or after April 8, 1966, of the Debentures with all coupons appertaining thereto, if any, maturing after the date fixed for redemption. Coupons maturing prior to the redemption date should be detached and surrendered for payment in the usual manner. The Debentures should be presented at The Chase Manhattan Bank N. A. (Corporate Agency Department), 80 Pine Street, New York, New York 10015.

CONVERSION RIGHT

Subject to the provisions of the Indenture, the holder of a Debenture is entitled at his option to convert such Debenture, or any portion thereof which is \$100 principal amount or a multiple thereof, into shares of Capital Stock of the Company. This right of conversion will terminate at the close of business on March 29, 1966. The conversion rate now in effect is 2 shares of Capital Stock for each \$100 principal amount of Debentures. As provided in the Indenture, no adjustment shall be made for interest accrued on any Debenture surrendered for conversion or for dividends on shares of Capital Stock issuable upon conversion of any Debenture.

From January 1, 1965 through March 3, 1966, the sales price for the Common Stock of the Company on the New York Stock Exchange ranged from a high of \$175.25 to a low of \$60.375 per share. On March 3, 1966, the last sale of such Common Stock on such Stock Exchange was at \$158.25 per share. So long as the market price of Common Stock is \$52.24 or more per share, a Debentureholder would receive, upon conversion of Debentures, Common Stock having a greater market value than the cash which such holder would receive if he surrendered Debentures for redemption.

The Boeing Company

By DEAN D. THORNTON, Treasurer

Dated: March 8, 1966

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Notices of the dates of the call and the expiration of the conversion privilege on March 29, 1966 were carried on the following services: NYSE ticker on March 8, 23, 24, 25, 26 and 28, 1966; NYSE Bulletin on March 11, 18 and 25, 1966; The Commercial and Financial Chronicle on March 14, 21 and 28, 1966; Standard & Poor's Bond Outlook on March 19, 1966; Standard & Poor's Called Bond Record on March 9, 11, 18 and 25, 1966; Moody's Industrial's on March 11, 1966. Articles about these dates were carried in the Seattle Post Intelligencer on March 25, 1966; the Seattle Times on March 27, 1966; and the Financial World on March 23, 1966. The notice also was carried in the Associated Press Bond Tables published on one or more days in at least 30 newspapers published in major cities across the United States.

On March 25, 1966, BOEING sent the NYSE certified copies of the Board Resolution and Chase Manhattan advised the Exchange that the necessary funds for redemption had been deposited with it. A further press release was sent to representatives of UPI and AP in Seattle and New York, and on March 28, 1966, in all editions of the Wall Street Journal and in the New York Times there appeared the following third notice:

"Final date for conversion of The Boeing Company's 4½% convertible subordinated debentures to Boeing common stock is Tuesday, March 29. . . . Closing price of the stock as of March 25 was \$154.5, representing a substantial advantage to holders of the bonds if the conversion is elected."

BOEING sought legal opinion from its counsel and from the attorneys for its investment bankers and was advised that the Wall Street Journal was a newspaper of general circulation in New York City and that the published notice of call met the requirements of the Indenture.

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Notice of the redemption was given all registered debenture holders and holders of coupon debentures registered as to principal by letter enclosing the notice published on March 8 and 18, 1966 (Section 5.02 Indenture). Neither BOEING nor Chase Manhattan gave notice of redemption by letter to any holders of unregistered bearer debentures.

It is of record that of \$21,514,700 face amount of debentures outstanding on March 8, 1966, \$19,970,300 or 92.8% were converted during the period following publication of the first notice of redemption on March 8, 1966 to and including March 29, 1966, and that more than \$9,000,000 of these were converted following the third publication of March 28, 1966. An additional \$115,400 were converted after midnight of March 29, 1966 upon request made to BOEING prior to that time and on a showing that there was a valid excuse for not meeting the deadline strictly. Of all the registered debentures totalling \$2,145,200, only three aggregating \$400 were not converted; and \$1,544,300 coupon debentures (of the class) were not converted.

It appears that discussion was had by BOEING about extending the deadline for exercising the rights of conversion. BOEING was advised by counsel that to do so would effect a change in the terms of the Indenture, and it had no legal right to this.

The Annual Report to stockholders of record for the year 1965, including a letter of transmittal from Allen, President of BOEING, dated February 28, 1966, was sent out between March 24 and March 30, 1966. The letter made no mention of the call, nor did a proxy statement, dated February 28, 1966, which was mailed between March 31 and April 4, 1966 to all stockholders of record as of March 10, 1966.

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The 8-K Form filed with the Securities Exchange Commission in February, 1966 made no mention of the proposed call, but it was reported in the 8-K Form of April, 1966.

Against these factual findings, I first consider:

THE NOTICE OF CALL OF THE DEBENTURES

In support of their claim that the notice of call was insufficient to bar the plaintiff-debenture holders from now converting, plaintiffs urge that the defendant had the duty to give notice which met the "reasonable expectations" of the debenture holders, because the Indenture was "a contract of adhesion".

"A contract of adhesion", a term used in reference to insurance contracts, is a contract drawn by one of the contracting parties in which the other party has no choice but to accept or reject (Williston on Contracts, 3rd Ed. 1961, 1971 Supp.; *Shay v. Agricultural Committee*, 299 F. 2d 516 (C.A. 9, 1962); and where the Court will ascertain that meaning of the contract which the weaker party would reasonably expect (*Gray v. Zurich Ins. Co.*, 54 Cal.2d 104, 419 P 2d 168).)

By this, plaintiffs urge that defendant BOEING should have done one or more of the following: (a) ascertained the names and addresses of the unregistered bondholders who presented their coupons for the collection of interest annually to Chase Manhattan; (b) traced the warrants which the stockholders had exercised in 1958 to purchase the debentures; (c) sent a letter to all stockholders of record and (d) placed an advertisement in the New York Times.

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The answer of the defendant, and one which I hold is conclusive, is that defendant was bound to give only such notice as was spelled out in the Indenture and in the Debenture, which incorporated the Indenture. This called attention to the Debenture for a definition of the rights of the respective parties and, in addition, repeated the terms of notice of call.

There is no claim here that the debenture or the Indenture provided such minimal notice as to constitute "ritualistic notice in small print on the back pages of a newspaper". (*Eisen v. Carlisle & Jacquelin*, 391 F. 2d 555, 569 (Ca.A. 2, 1968).) The notice required was not only adequate, but the defendants did more than was required when they published a third time on March 28, 1966 in all editions of the Wall Street Journal and in the New York Times, with the "dramatic and widespread rippling effect" which brought in over 9,000,000 face amount of debentures for redemption. In fact, the very minimal aggregate number of non-converting debenture holders, which constitute the class represented, speaks eloquently for the adequacy of notice given by defendants.

The suggestions made by plaintiffs as to the further notice which might have been given are not only not required by the terms of the Indenture but they would have been impracticable, if not impossible. The warrants, as well as the bearer debentures, were traded repeatedly since 1958, so that it would have been impossible to know in 1966 the names and addresses of the debenture holders. It was stipulated that, of the debentures issued totalling \$30,597,600 during these years, \$68,694,000 were traded; and

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that of a total of 7,037,448 rights issued, 1,702,200 rights were traded between July 16 and 28, 1958; as for the stockholders numbering about 50,000, 55% of these had stock in a street name.

Nor would the coupons presented for payment give the names and addresses of the debenture holders. The greater number of these were presented through collecting banks and, although BOEING might have ascertained the owners through the banks, it was under no duty to do so.

Plaintiffs' argument that the majority of the debenture holders never saw the Indenture as they would have had to go to the Trustee or to the Securities Exchange Commission in Washington, is answered by the fact that the debenture itself contained the provisions for notice and the warning that the debentures could be called, as well as by law on the binding effect of the terms of the Indenture as a contract, whether or not they saw it. (*York v. Guaranty Trust Company of N.Y.*, 326 U.S. 99; 143 F. 2d 503 (C.A. 2, 1944); U.C.C. Sec. 8-202(1) 2d ed.)

But plaintiffs further argue that the debenture holders are not bound by the terms of the Indenture because these terms were inconsistent with those of the debenture and the Prospectus which accompanied the issue in 1958. Thus, they purport to find some inconsistency in the words "not less than 30 days' notice nor more than 90 days published notice" (Prospectus); "not less than 30 nor more than 90 days prior notice as provided in the Indenture" (debenture); and "the first such publication to be not less than 30 days and not more than 90 days before the date fixed for redemption"

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(Indenture Section 5.02). They argue that the plaintiffs, as debenture holders, might have thought that this meant 30 days' continuous publication and that any doubt must be resolved in their favor. The language is pristine clear—30 days' prior notice; this was what was given, and more.

Kaplan v. Vornado, 341 F. Supp. 212 (N.D., Ill., 1971) is dispositive of this claim. There, in answer to the same argument, the Court held that the debenture holder was bound by the terms of the Indenture, which he did not see, as well as by the terms of the Debenture, which he did not understand; and that the notice was sufficient, even though it was published in a New York newspaper and in various publications which plaintiff, a resident of Kansas, never saw.

In *Abramson v. Burroughs Corp.*, 67 Civ. 1426 (S.D. N.Y., 1972), Judge Lumbard held that notice by publication in the New York Times and the Wall Street Journal was reasonable as "best calculated to come to the attention of the Burroughs bondholders" or their brokers, and that publication four times within the thirty days prescribed by the Indenture, with termination of the privilege the fifteenth day prior to the redemption date, was sufficient notice (*Mullane v. Central Hanover Trust Co.*, 339 U.S. 306 (1950) and the other cases relied on by plaintiffs are not relevant in that, in those cases, the Courts struck a notice by publication as insufficient to bar a party in a judicial proceeding where another kind of notice was possible. *Walker v. Hutchinson*, 352 U.S. 112 (1956) condemnation proceedings; *New York v. N.Y. Central R.R. Co.*, 344 U.S. 293 (1953) wiping out a tax lien in a bankruptcy proceeding.)

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Finally, plaintiffs argue that the defendant violated the Trust Indenture Act, 15 U.S.C. Section 77aaa et seq., in that, under the Indenture by Section 8.01, 8.02, BOEING was required to furnish Chase Manhattan bi-annually with current names and addresses of bondholders and that this would have permitted Chase Manhattan to notify those additional bondholders. The answer to this is that it was stipulated that BOEING had no names to furnish Chase Manhattan and so advised it under the terms of the Indenture.

Plaintiffs held the debentures which clearly stated that they could be registered; plaintiffs could have done so and they would have been notified by mail of the call thus eliminating the real risk of not seeing the notices and press releases. Plaintiffs chose not to do so, and they must bear the consequences (*Kraus v. Laclede Gas Co.*, 354 S.W. 2d 327 (St. Louis Ct. of App., 1962)).

I conclude that the notice of call was reasonable, valid and adequate.

I now turn to consideration of:

THE CONVERSION RATE

In an ingenious argument, in order to get around the sufficiency of the notice, plaintiffs next argue that it was a condition precedent to a valid call that defendants adjust and publish an adjusted conversion rate and notify the Trustee; that defendants did not and that this rendered the call invalid and insufficient to cut off debenture holders' right to convert.

The defendants' rejoinder is that the rate of conversion fixed by it was in strict compliance with the terms of the Indenture and that these

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should not be rewritten to support the plaintiffs' claim; that the Board of Directors made its determination as to the conversion rate with due regard to its dual responsibility to both stockholders and bondholders; that, in any event, an error in the conversion rate would give a claim to those bondholders who did convert relying on the notice and not to plaintiffs who claim they received no notice of the conversion.

Solely for purposes of discussion, I will assume that an error in the conversion rate would void the call and that such an error, even though I find none, would be sufficient to save plaintiffs' claim. I turn to that aspect of this suit, and consider the merits of this claim.

There were three transactions which, according to plaintiffs, might have necessitated an adjustment in the conversion rate applicable to the debentures in accordance with Section 4.05 of the Indenture: the 4% stock dividends declared in November, 1958; the 2% stock dividend declared in November, 1959; and the acquisition by BOEING on March 31, 1960 of substantially all of the assets of Vertol Aircraft Corporation.

As of March 10, 1961, up to and including the redemption date of April 3, 1966, BOEING treated the conversion rate as 2.0448, and it contends that this is the proper conversion rate. It is plaintiffs' contention that the proper conversion rate is 2.0725 or more. The significance of this is that, if plaintiffs are right, the debenture holders would have been entitled to additional shares of stock on conversion and additional duties were imposed on defendant under the Indenture which they did not fulfill.

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Essentially, it is plaintiffs' contention that initially BOEING computed the value of the 4% stock dividend correctly, but that the following year it recomputed it for the express purpose of keeping the conversion rate from rising above 2.5 at a time when it was negotiating with Vertol in order to injure the debenture holders and benefit its stockholders.

It is of record that on November 3, 1958, BOEING declared a limited stock dividend of 4%. The closing price of Boeing Capital Stock on that date was \$56.875 and the number of shares issued under the 4% dividend was 281,537. On or about December 31, 1958, BOEING made a conversion rate computation with respect to this 4% limited stock dividend. BOEING took the November 3, 1958 NYSE closing price of \$56.875 and divided it by 1.04 (representing the number of shares including the 4% dividend shares) and reached a figure of \$54.75 which was the value of each share after dividend. This figure, multiplied by the number of shares issued, 281,537, resulted in \$15,414,151—the total consideration paid for the shares issued. Applying the formula for calculating the conversion rate, the "Conversion Rate Calculator" (Section 4.05), it reached a figure of 1.9927. The numerator being 731,898,400, total number of shares outstanding, divided by the denominator, the total consideration received therefor or \$367,286,501, the conversion rate, therefore, was below 2.05 and it required no adjustment.

On November 2, 1959, BOEING declared a limited stock dividend of 2% and issued 147,489 shares at the market price of \$30.375 or a total consideration of \$4,479,979.

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For purposes of this dividend, however, BOEING, in computing the consideration received for the shares, did not divide the market price \$30.875 by 1.02 (to include the 2% dividend shares) because if it had, the consideration would have been reduced to \$29.77 which result would have required an adjustment in the conversion rate since that quotient would have been 2.0089 instead of 2.0052.

In December, 1959, BOEING then recomputed the 4% limited stock dividend of 1958 to conform to the computation used on the 2% dividend and to exclude the additional 4% shares represented by the dividend so that now it reached a flat market price of \$56.875 (not divided by 1.04). The result was that the total consideration for the 281,587 shares issued was \$16,012,417, which under the formula still did not change the quotient sufficiently to require adjustment of the conversion rate.

A tabulation of these calculations is as follows:

4% dividend—281,537 shs.	x \$54.69	= \$15,414,151	(corporate accounting method)
"	x \$56.857	= \$16,012,417	(Indenture method)

2% dividend—147,489 shs.	x \$29.77	= \$ 4,390,748	(corporate accounting method)
"	x \$30.375	= \$ 4,479,979	(Indenture method)

Quotients computed according to Section 4.05 of the Indenture:

Quotient for 4% dividend under either method below 2.05: 1.9927; 1.9895

Quotient for 2% dividend under Corporate Method = 2.0089

Indenture Method = 2.0052

(See Defendant's Exhibit No. 20)

Obviously, one of the reasons for the recomputation of the "Conversion Rate Calculator" on this dividend was to conform it to the method used on the 1959 2% stock dividend.

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From this, plaintiffs argue that defendant was on a course of deliberating keeping the conversion rate from going up, which would require an adjustment and the setting aside of more shares for the debenture holders when they redeemed their debentures.

Irrespective of the defendant's motive, it is clear that the original computation of the 4% limited stock dividend was not proper under the terms of the Indenture and that the computation of the 2% dividend and the recomputation of the 4% dividend in 1959 was in accordance with the terms of the Indenture. It appears that the 4% stock dividend was originally in 1958 computed according to the usual corporate accounting practice, that is, that the market value of the stock issued was computed by including the additional number of shares outstanding upon payment of the dividend. In the case of the 4% stock dividend, this would be 104 shares and, in the 2% dividend, 102. The terms of the Indenture are clear in that the market value of a limited stock dividend is defined as the last reported sales price on the date of the declaration of the dividend (Section 1.01). Plaintiffs would construe this to mean that this includes the sales price including the additional shares issued as a result of the dividend, or post dividend rather than ex-dividend, arguing that this is the more intelligent meaning because it represents more accurately the market value of the shares. This may be so but the Indenture was drawn by BOEING; how to define market value was its decision to make out of several alternatives. BOEING had a right to so define it, and, having done so, it had not only the right but the duty to comply with the definition set forth in the Indenture, irrespective of its motive.

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Plaintiffs also attack the acquisition by BOEING of the assets of Vertol Aircraft Corporation at what they say was an arbitrary value placed on the stock of BOEING which was issued in exchange, in order to keep the conversion rate below 2.05.

In support of their position, plaintiffs point to the statement made by Vice President Haynes at a Board Meeting on April 4, 1960 after the contract with Vertol had been signed, that:

"a calculation had been made as to the minimum value that could be placed on the assets of Vertol without an adjustment in the conversion price being required; and that such figure as adjusted for the amounts to be received upon the exercise of options was approximately \$15,216,000."

and to further statements by BOEING's officers that their "basic objective was to avoid dilution of the equity position of the stockholders."

The value placed on the Vertol acquisition was the market value of the BOEING stock on November 18, 1959 at \$33- $\frac{5}{8}$ for a total of \$15,895,748.

It is plaintiffs' argument that some other valuation should have been used, either the value of the acquired assets of Vertol on March 31, 1960 as recorded on the books of BOEING at \$12,485,188.47 or the value of the BOEING stock at some other date, to wit: either January 18, 1960, when the contract was signed when the stock was \$30- $\frac{5}{8}$; or March 30, 1960 when the contract was closed when the BOEING stock was \$24- $\frac{7}{8}$; either of which figures would have required an adjustment in the conversion rate.

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Defendants rely on Section 405(b) (ii) of the Indenture which vests the Board of Directors with the power to fix the "fair value" of the consideration received when stock is issued other than for cash. Defendants represent that the decision of the Board was made after full deliberation, in good faith, with full realization of its duties to the stockholders of BOEING, and upon advice of counsel, its investment bankers and independent accountants.

I find that the facts are as follows.

As early as 1958, BOEING's management had been engaged in discussions with Vertol looking toward the possible acquisition by BOEING of Vertol. A committee, headed by the Company Secretary, was designated to study the matter and recommend; on November 11, 1959, a memorandum containing his and the President's recommendations was sent to the Board. The recommendation was for the acquisition on the basis of an exchange of stock—two shares of BOEING for three shares of Vertol. On November 13, 1959, at an informal meeting of nine of BOEING's thirteen Directors, attended by its President Allen, a firm decision to make the offer to Vertol on the two for three basis was made. On January 18, 1960, the Board formally authorized the execution of a contract with Vertol; the closing was had on March 31, 1960. Between November 13, 1959 and January, 1960, there were several discussions as the details were still tentative. Throughout these negotiations and meetings, defendants were figuring out various valuation theories to determine the result on the conversion rate.

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The acquisition was done through a corporate reorganization in which the stockholders of Vertol received two shares of BOEING stock for each three shares of Vertol stock they owned, and received a total of 448,954 shares of BOEING capital stock. There were also Vertol stock options, which had been granted to employees at a prior time. These stock options amounted to 28,782 shares of BOEING at a value of \$644,514; and the total consideration paid by BOEING for the acquisition was 472,736 shares of BOEING at 33- $\frac{1}{8}$, for an aggregate value of \$15,895,748.

This is known as the "barter equation method", which permits consideration to be computed on the basis of shares issued.

The book value of Vertol at \$12,435,138.47 was the figure used for the computation of the Pennsylvania State Excise Tax; had BOEING used this value, an adjustment in the conversion rate would have had to be made. Using the value of BOEING stock at 24 $\frac{1}{8}$ as of March 30, 1960, the quotient after applying the formula would have been 2.0687 requiring an adjustment to 2.07 shares; at the value used of \$15,895,748 or \$15,250,000 (which excluded the options), the quotient remained below 2.05. Thereafter, BOEING continued to use this method of computation for limited stock dividends under the Indenture, with the approval of its independent accountants, its counsel and its Company treasurer.

Plaintiffs admit that the formula provided for in the Indenture had as its purpose the prevention of dilution of stock to the detriment of BOEING stockholders. It was certainly BOEING's duty and right to compute

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stock in such a way as to prevent its dilution and there is no evidence that it had any purpose of deliberately hurting its debenture holders.

While it is true, as plaintiffs point out, that on November 13, 1959 the matter of the acquisition was still tentative and does not appear to have been settled until some time in December at the earliest and that the date the contract was signed appears more rational, this Court cannot say that the Board of Directors had no colorable right to fix the "fair value" of the consideration as of November 13, 1959. The decision was carefully taken, not only with the approval of its accountants but of independent auditors, outside counsel, its investment bankers and underwriters, with the unanimous resolution of its Board and in good faith. This is the test rather than whether another method of valuation might seem more appropriate. In fact, plaintiffs admit that they can cite no authority which deals with the fixing of a date for purposes of valuation of antidilution clauses, which this is. As plaintiffs point out, any time stock is issued for consideration less than its market value, there results dilution. The provisions of Section 4.05 of the Indenture were clauses dealing with the problem. There is ample authority to support a decision made by a Board of Directors under similar conditions; in fact, it is conclusive. [*Morris v. Standard Gas & Electric Co.*, 31 Del. Ch. 20, 63 A 2d 577 (1949); 11 Fletcher Corporations, Secs. 5221, 5336, 5344, (1971); *Industrial & General Trust, Ltd. v. Tod*, 180 N.Y. 215 (1905). See *Matter of Marcus*, 273 App. Div. 725, affd. 303 N.Y. 711 (1951) to the effect that book value is not the true measure of stock; and *Seas Shipping Co. v. CIR*, 371 F. 2d 528 (C.A. 2) cert. denied 387 U.S. 943, for use of

Opinion of Ryan, D.J. Dated November 29, 1973

the barter equation method for tax purposes.]

I conclude that neither the 4% nor the 2% Limited Stock Dividend, nor the acquisition of Vertol, nor any combination of these three events, required an adjustment of the conversion rate. I also conclude that, even if they had so required it and defendant had failed to do so, plaintiffs who did not convert could not benefit thereby because failure to convert when required to do so would not necessarily have invalidated the call. [6 Williston on Contracts, Sec. 842 (3rd Ed., 1962).]

I also conclude that there is no merit or substance to plaintiffs' final point that the defendant BOEING breached a contract it had made with the New York Stock Exchange, in that it failed to comply with the publicity requirements of the Manual and/or the Listing Agreement.

I have found that the publicity given was more than adequate, that it was in full compliance with the terms of the Indenture and the Debenture, and that is the only contract between plaintiff debenture holders and BOEING. The fact that further publicity was suggested or even required under the Manual of the Exchange, assuming it was a contract, would not help plaintiffs for defendant BOEING did comply with the publicity requirements of the Exchange. But even if it had not complied fully with the publicity requirements of the Manual, no case has yet held that the Manual is a rule of such importance in the "Regulatory Scheme" and as such "integral part in SEC Regulation" that a breach of it would expose defendant to "unexpected civil liability" at the suit of a third party. (*Weinberger v. NYSE*, 385 F. Supp.

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189 (S.D.N.Y., 1971).) In fact, the law in this Circuit is to the contrary. (*O'Neill v. Maytag*, 389 F. 2d 164 (C.A. 2, 1964); *Colonial Realty Corp. v. Bache & Co.*, 358 F. 2d 178 (C.A. 2, 1966); *DeRenzi v. Levy*, 297 F. Supp. 998 (S.D.N.Y., 1969).)

Buttrey v. Merrill, Lynch, etc., 410 F. 2d 185 (7th Cir., 1969), cert. denied 369 U.S. 848, relied on by plaintiffs, involved a totally different "rule" of the Exchange binding on a member company and plaintiff's claim against the member broker was upheld in the pleading stage solely because it charged the member company with fraud; the Court specifically saying that mere negligence might not support a federal claim. [*McMaster, Hutchinson & Co. v. Rothschild Cor.* C.C.H. Fed. Sec. L. Rep. #98,541 (N.D., Ill., 1972) which followed, distinguished *Buttrey* on this ground; *Bush v. Bruns, Nordeman & Co.* (S.D.N.Y. 72 Civ. 484) C.C.H. Fed. Sec. L. Rep. #98,674.] What I have said disposes of plaintiffs' third party beneficiary claim.

The Clerk is directed forthwith to enter judgment for defendants dismissing the complaints in the following ten actions on the merits with taxable costs and disbursements:

- | | |
|-----------------------------------|---------------------------------|
| 66 Civ. 1820 Van Gemert v. Boeing | 66 Civ. 3005 Diener v. Boeing |
| 66 Civ. 2384 White v. Boeing | 66 Civ. 3054 Finn v. Boeing |
| 66 Civ. 2385 Berglas v. Boeing | 66 Civ. 3403 Mittler v. Boeing |
| 66 Civ. 2640 McNaught v. Boeing | 67 Civ. 280 MacMillan v. Boeing |
| 66 Civ. 2786 Winer v. Boeing | 67 Civ. 1053 Hoff v. Boeing |

So ordered.

Dated: New York, New York
November 29, 1978

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SYLVESTER J. RYAN
United States District Judge

COPY RECEIVED
THIS 10 DAY OF Oct 1974

RASS, GOODKIND, WEISLER & GERSTEL
Attorneys for Plaintiff

(received 3 copies)

Received 3 copies Oct 10 1974
Nathan, Mandelbaum, Asche, Wexler &
Friedman, attorneys for Committee
of Plaintiffs

Jury Steiner Atty for
Committee of Plaintiffs Received 3 copies
Oct 17 1974